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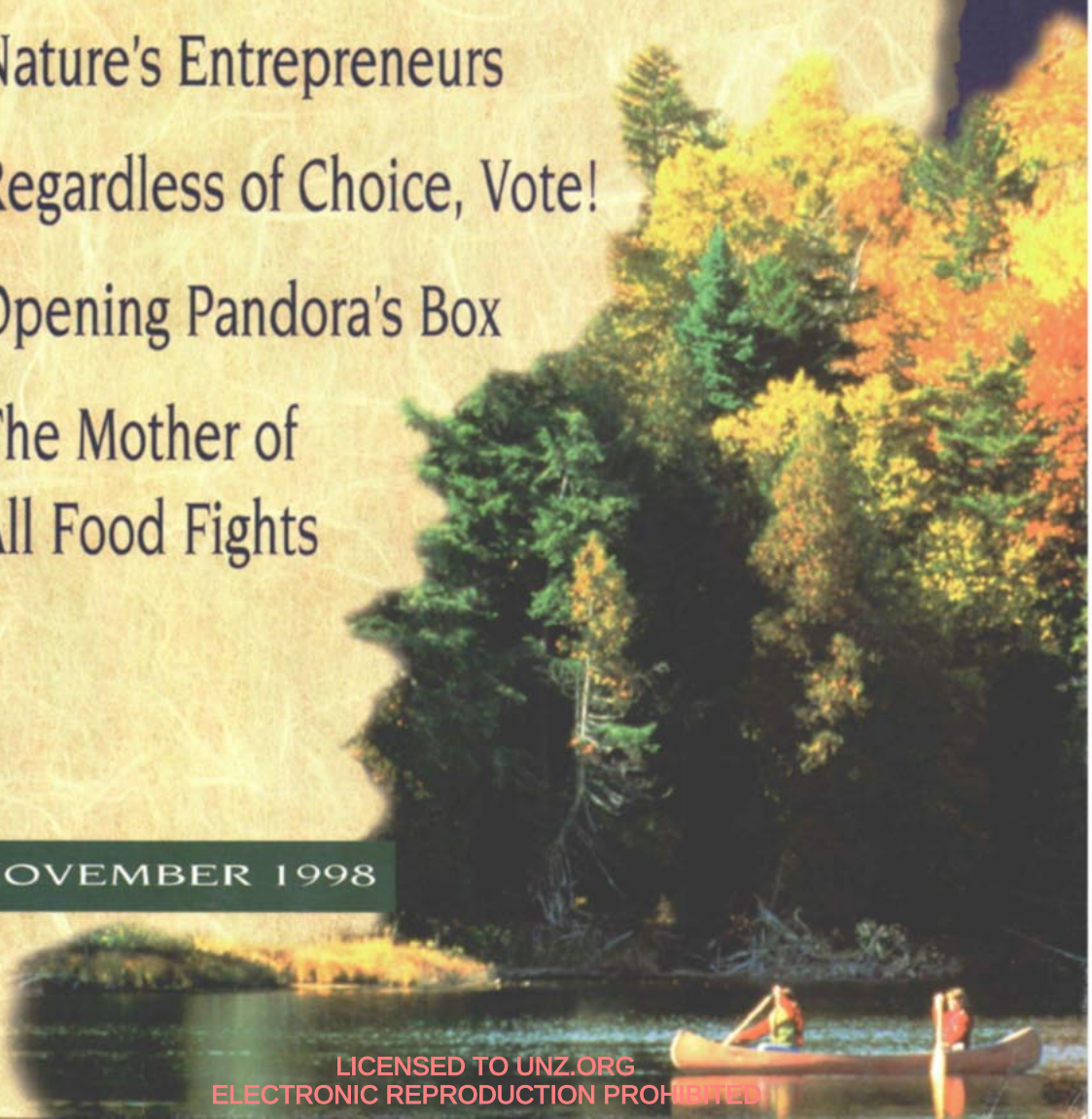

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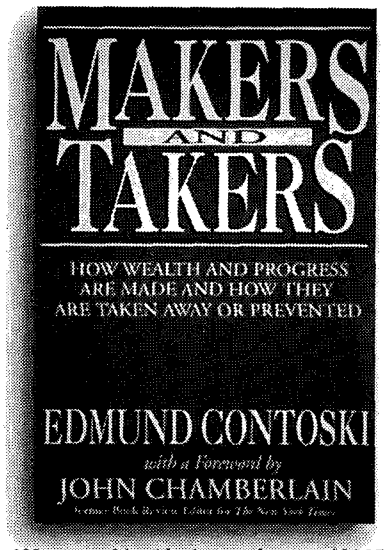

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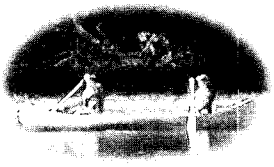

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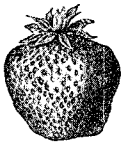

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PERSPECTIVE

The Great Pretenders

William McChesney Martin, Jr., who was chairman of the Federal Reserve from the Truman through the Nixon years, died last summer. According to the *New York Times* obituary, Martin hated inflation and deficits. Further, he had a reputation for jealously guarding the Fed's independence and resisting presidential and congressional pressure to lower interest rates. Before taking the Fed's helm, he was the first paid president of the New York Stock Exchange, and after World War II, he ran the Export-Import Bank. His father, a St. Louis banker, helped draft the Federal Reserve Act for President Woodrow Wilson and served as president of the St. Louis Fed.

Ordinarily, we wouldn't take note of the passing of a retired central banker, but Martin said something that deserves recognition here. In a 1985 interview with the *Times* he recalled his early days running the Fed, at which time he said to himself:

> My gracious, here I am the new chairman of the Fed and I'm doing my best—I'm not the brightest fellow in the world, but I'm working hard on this—and *I haven't the faintest idea of how you figure the money supply*. Yet everybody thinks I have it at my fingertips. [Emphasis added.]

Then Martin told the *Times*: "They don't really know what the money supply is now, even today. They print some figures—I'm not trying to make fun of it—but a lot of it is just almost superstition."

It is interesting to have someone like Martin confirm what many advocates of free banking have long claimed, namely, that central bankers are much like the Wizard of Oz. Behind the awesome display of apparent power and wisdom are a few well-intentioned, fallible human beings pulling levers, turning wheels, and pretending to know things they can't possibly know.

* * *

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Advocates of the command-and-control approach to environmental issues implicitly assume that there is no commercial reason for entrepreneurs to preserve wilderness areas and other potential recreational amenities. In an excerpt from their recent book, *Enviro-Capitalists*, Terry Anderson and Donald Leal show that, in fact, reasons abound.

In our reprint honoring the 100th anniversary of his birth, FEE founder Leonard Read speculates about what would happen if we voted "by turning our backs" on irresponsible candidates.

The days of government fiat money may be numbered. What could hasten the end of this most mischievous form of intervention? Technology, explains James Dorn.

The Internet has its roots in a computer network funded by the federal government to link defense researchers around the country. That origin has been cited in support of a variety of government-financed projects. Andrew Morriss says there's a lot more to the story.

The antitrust suits against Microsoft have come in for much criticism. But PC-industry pioneer Dan Fylstra asks a novel question: wouldn't there be more to fear from a wealthy Microsoft in a regulated computer industry driven by political influence?

The U.S. Department of Agriculture wants to define the term "organic food." As Sam Kazman shows, that's almost as if the government had decided to define the one true religion. There's trouble ahead.

Senate hearings on Internal Revenue Service abuses have yielded yet another taxpayer-protection law. But if the past is any guide, James Bovard writes, skepticism is in order.

During the recent unsuccessful attempt to raise the minimum wage, Democrats claimed it would help low-income workers. Republicans said it would throw people out of work. It's not that simple, says Richard McKenzie.

A growing movement believes that corporations should do more than merely make money for their shareholders. Even some businessmen take that position. John Hood untangles the issues that make up the corporate-responsibility crusade.

Government regulation burdens business, particularly small business. And as Ray Keating demonstrates, it often creates an irresistible incentive for small businesses to stay small.

Many states of the Union are going after the tobacco industry to recover money they've spent on citizens' smoking-related ailments. Daniel Hager asks why state governments are entitled to recovery, considering that it's not their money and that one person's medical bill is several persons' windfall.

Columnist Lawrence Reed discusses the horror of civil-asset forfeiture. Doug Bandow considers the spectacle of a group of old people who miss the Bolsheviks. Dwight Lee argues that government price ceilings really can't lower the cost of products. Mark Skousen continues his series on gold. And Charles Baird explains why workers in California lost a chance to stop unions from spending their money on politics. Immigration harms the environment? Turn the page to see why "it just ain't so."

Books by Richard Rorty and Michael Lind come under the watchful eyes of our book reviewers, along with works tackling the subjects of sports subsidies, American cities, individualism, the war against the automobile, and predatory tax policies.

—SHELDON RICHMAN

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Ideas On Liberty

It Just Ain't So!

Since ancient times people have been fretting about overcrowding the earth. In 1798, Thomas Robert Malthus was already a latecomer to the alarmist message that mankind would breed itself into extinction. He was far from the first Malthusian. (It's widely unappreciated that Malthus revised later editions of his *Essay on the Principle of Population* because he had forgotten something that changed his whole analysis: "moral restraint," or the power to control reproductive activity. And that was before the invention of contraception.)

That people worried about overpopulation when the human race numbered under a billion should cast a certain light on the periodic warnings in our own time that we face a dire threat. The late Julian Simon single-handedly created a body of work that blasts the foundation of these warnings to smithereens, but for some people, feeling bad feels so good. They are reluctant to consult the evidence when there is a risk that they will have to abandon their visions of the apocalypse.

Environmentalist Bill McKibben furnishes the latest jeremiad about overpopulation. Several months ago McKibben, author of *Maybe One,* a case for one-child families, presented his argument for controlling population to readers of the *New York Times* op-ed page. The context was the immigration issue. Environmentalists have a tough time with that one. Some, like the members of the Sierra Club, don't want to talk about it. While they believe immigration is bad ecologically, they don't like the company they'd be in if they opposed it outright. They can't bring themselves to tell the "tired . . . poor . . . masses yearning to breathe free" to stay where they are. Yet the environmental lobby is clearly uneasy at the prospect of their coming here. We have too many people already.

McKibben shares this ambivalence. In his misleadingly titled article, "Immigrants Aren't the Problem. We Are" (in fairness, the title was probably written by a *Times* editor), McKibben says, "Immigration is about as difficult a moral subject as one can imagine. . . . In a world of desperate poverty, it is hard for citizens of the richest nation to argue that the door should be closed, especially since nearly all of us can recall our immigrant roots." But how can we accommodate them? Even living "more simply" won't help. Our "sheer numbers," the result of longer life spans and the baby boom, are the problem. Americans may be reproducing below the replacement rate of 2.1 children, but that's not good enough. (Europeans are having even fewer children than Americans are, alarm over which recently made page one of the *Times*. Are the opinion-molders signaling a new agenda, subsidies for having children?)

McKibben could support a halving of the annual immigration rate, to 400,000. But he's suffering a case of conscience. How can we do that, he asks, if we are not willing to impose a little discipline on ourselves? "If, however, we are willing to take some painful steps ourselves, then we earn the right to tell some tough truths to others—chief among them that even this rich land can't grow forever."

"Painful steps." The population-alarmist literature always seems to contain that phrase.

McKibben sees two problems. First, the country is too crowded: "The Northeast corridor of suburbs and cities is already more densely populated than Haiti or El Salvador; California's 30 million may become 50 million by 2050."

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Meaning what? Are Haiti and El Salvador poor because they are crowded? Hong Kong, Taiwan, Singapore, and Monaco are far more "crowded," but they are not poor. Some of the most destitute areas, such as Chad and Somalia, are also the most sparsely populated places on earth. The underdeveloped world may have lots of reasons for its poverty, but population isn't one of them.

"That endless growth places real stress on our supplies of everything from water to silence, from farmland to solitude," McKibben writes. This is just wrong. As Julian Simon so often pointed out—and won a bet doing so—we aren't running out of things, at least not the things subject to market pricing. Raw materials are cheaper and more plentiful than ever. A gallon of gasoline, that quintessential nonrenewable resource we were running out of a few years ago, is cheaper than a gallon of milk! As for a shortage of solitude, the communitarians lament that we are all ignoring our neighbors and bowling alone (or sitting at the PC). In the most "crowded" parts of the United States, individuals have more private living space than ever. You can find silence if you want it. (I'm writing this in a suburb of Washington, D.C., and all I hear are birds and insects.) Let's not forget that people pay a premium to live in the most "crowded" parts of the United States.

McKibben's second point is that "Americans, as the world's most voracious consumers, contribute far more per capita to the world's environmental problems than anyone else." And the cars and homes are getting bigger still, he says. This sort of analysis usually winds up with an attack on consumption. But the economics is off base. Consumption need not damage the earth—quite the contrary. Our desire for more things, combined with natural market incentives, impels us to find ways to get more from less, which is exactly what we have done for generations. And as we get richer, we have more time for recreation; that often means increased demand for parks, wilderness, and beaches.

McKibben needs to resolve this paradox: how can we be consuming more while not running out of anything? There's an answer, but to get at it, one must give up the environmentalist assumption of fixed resources. Ultimately, resources are the products of intelligence, the supply of which is not fixed.

Without their theory of the malignancy of consumption, however, the environmentalists would have no case to reduce immigration. Immigration does not increase total world population. In fact, it could reduce future growth because people in rich countries tend to have fewer kids than people in poor countries. But McKibben says that "If those who wanted to immigrate here stayed instead in Juarez or Shanghai or, for that matter, Dublin, they would do far less damage to the planet precisely because they would not be as rich."

There it is. The poor must remain poor because to be rich is to destroy the planet. But if that is so, why is it that in the richest, and freest, countries, people live the longest, healthiest lives and have the cleanest living conditions? In the poorest places, people are at risk of dying from airborne and waterborne diseases and unsanitary conditions. If you want to see environmental damage, look at the places where governments control production and consumption in the name of the common good.

It's the desire and the freedom to produce and consume that have made the West wealthy. And as the late Aaron Wildavsky so often said: wealthier is healthier. □

—SHELDON RICHMAN

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THE FREEMAN
Ideas On Liberty

Nature's Entrepreneurs

by Terry L. Anderson and Donald R. Leal

> "We have our idealists, inventors, innovators and organizers all around us, and in a vast mechanism of economic and social change there is work for all kinds to do. . . ."
> —JONATHAN HUGHES, *The Vital Few*

In his book *The Vital Few*, Jonathan Hughes describes the entrepreneurs of the late nineteenth and twentieth centuries who unleashed America's industrial power. Names like Rockefeller, Vanderbilt, Carnegie, Ford, and Morgan lead the cast of characters. In some cases these "vital few" invented new products or production techniques, but mostly they amassed capital, contracted with other input owners, and developed marketing strategies that lowered the cost of products and increased profits. In recent times, industrialists may have fallen from the list of the vital few, replaced by electronic-information gurus like Bill Gates or media moguls like Ted Turner, but the required entrepreneurial skills remain basically the same.

It is impossible to predict the frontiers on which the next wave of entrepreneurs will leave their mark. One possibility is the environment.

It is worth asking what it takes to be a successful entrepreneur in the environmental arena. If we were to compile a list of the vital few from the environmental history books, it might be headed with names like Audubon, Leopold, and Muir. As entrepreneurs, these men recognized the value of the natural world at a time when most people saw nature's frontier as a wilderness to be tamed. Of these early entrepreneurs, however, only Aldo Leopold saw the importance of linking the conservation movement to entrepreneurship, with all the trappings of finance, contracting, marketing, and even profits.

Unfortunately, many of today's environmentalists have not picked up where Leopold left off. His entrepreneurial spirit has given way to political opportunism. Instead of business acumen, the vital few in the environmental movement understand politics, lobbying, and fund-raising as the tools to achieve their political objectives. The headquarters for most major groups are located in Washington, D.C., and the personnel spend their time in the halls of Congress rather than in the wilds of nature.

The campaign to "save" the African elephant illustrates how political and financial

Terry Anderson is a professor of economics at Montana State University and executive director of the Political Economy Research Center in Bozeman, Montana. Donald Leal is a senior associate of PERC. This article was adapted from chapter one of their book Enviro-Capitalists: Doing Good While Doing Well. *Copyright 1998 Rowman & Littlefield.*

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agendas can overtake environmental realism. Though more than one million elephants roam southern Africa, environmental leaders of groups such as the Humane Society of the United States and the World Wildlife Fund declared elephants an endangered species and instituted fund-raising campaigns, publicized with vivid pictures of slaughtered elephants, tusks removed by chain saws. They raised millions of dollars to promote a ban on trade in ivory, although many African conservationists believed this would only further drive up the price of ivory and increase poaching. Rather than channeling their efforts into the direct protection of elephant habitat, these leaders politicized the elephant issue and motivated politicians and bureaucrats to ban trade in elephant products through CITES (Convention on International Trade in Endangered Species). They gave little consideration to the incentives faced by African natives who directly bear the costs of living with the elephants. These people, many of whom live at subsistence levels, are being asked to preserve habitat, let their crops be destroyed, and perhaps even be killed to save elephants because Westerners living in comfort thousands of miles across the ocean think it is a good idea. These political entrepreneurs demand the protection of elephants but place the burden of their protection on the backs of those who can least afford it. In the end, the campaign to "save" African elephants by banning trade in ivory filled the coffers of Western environmental groups. Unfortunately, it reduced the potential for Africans to live in harmony with elephants because it prevented the indigenous population from profiting from good stewardship.

Enviro-Capitalism

There is an alternative approach—enviro-capitalism—that begins when environmental entrepreneurs discover new opportunities for improving environmental quality and then figure out how to produce it in the private sector. Enviro-capitalists are entrepreneurs using business tools to preserve open space, develop wildlife habitat, save endangered species, and generally improve environmental quality. These entrepreneurs are meeting the growing demand for recreational and environmental amenities. To do this, enviro-capitalists must invent new products, attract venture capital, contract with resource owners, and market their products. The enviro-capitalist encourages fee hunting to reward landowners for bearing the cost of providing habitat for wild animals; buys endangered-species habitat instead of lobbying for regulations that restrict the use of private lands; and leases water to increase instream flows, rather than seeking legislation to limit water use by irrigators. In meeting each of these human demands, enviro-capitalists also benefit the environment.

People are beginning to realize that markets can be a powerful force in the environmental movement. Market-based incentives have become a common approach in both the private and public sectors. Corporations are searching for ways to increase profits in environmentally friendly ways. Policymakers are facing the reality that a cleaner environment comes at an increasingly higher cost. By harnessing market forces as enviro-capitalists do, we can achieve environmental ends at a lower cost.

With rising incomes, the demand for environmental amenities grows. The question is who will meet those demands, politicians or enviro-capitalists.

More Than Paper Profits

Tom Bourland, wildlife biologist and entrepreneur, preaches that the market can be wildlife's best ally. He believes that the growing demand for wildlife and recreation provides landowners with powerful incentives to produce more wildlife habitat and more recreational opportunities. And he should know, having turned wildlife into a money-maker for International Paper (IP), one of the largest timber producers in the United States.

In the early 1980s, Bourland became a wildlife manger of 1.2 million acres of IP's timber-producing land in its mid-south region, including parts of Texas, Louisiana, and Arkansas. When he joined the company, its wildlife and recreation program was not

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designed to generate income but rather to keep neighbors happy, appease environmentalists, and stem the rising tide of government regulations placed on private timber owners. Bourland was hired as a token wildlife biologist to operate within this agenda, but he was quickly frustrated—the bottom line on the financial statement was driven by timber production.

Recognizing the importance of the profit motive, Bourland locked his entrepreneurial radar onto the relationship between wildlife and IP's financial statements. He noted the growing demand for hunting, fishing, and recreation, as well as the consumers' willingness to pay for quality experiences. But he also saw that the company was receiving nothing for the use of these amenities. Bourland's environmental agenda had to give way to new realities. To respond to these realities, the company's wildlife and recreation program had to earn its way by charging user fees of those enjoying the amenities on IP's lands.

Charging fees for recreation represented a bold move for a timber company because it was bucking tradition. In the rural townships of Louisiana, Bourland's home state, local people were accustomed to hunting, fishing, and camping for free on IP's lands. Some did not take kindly to having to pay. Indeed, some regional managers at IP worried that they would be the ones facing the wrath of a disgruntled public. According to IP's then-chairman and chief executive, John Georges, "There were times when some executives were asking, 'Is it worth it—should we be doing this?'"

Despite local objections, IP proceeded with the change, spurred by several factors. Besides evidence of growing recreational demand, increasing abuse on IP's open lands was costing the company dearly. Litter, arson, and off-road traffic were major problems. Also, wildlife populations were declining from years of poaching and excessive legal hunting. Hunters were complaining about too little game and too many people.

Bourland and other supporters of fees at IP argued that revenues from wildlife and recreation would more than offset the additional costs of monitoring IP's lands and improving conditions for wildlife. They believed that fees for land use provided an effective strategy that would create stronger incentives for users to care for the land. A major part of the fee program included selling multiyear land leases to hunting clubs. Under the lease arrangement, clubs have a personal stake in stewardship of "their" areas. Bourland believed that clubs would monitor land use, limit hunting pressure, and cooperate with wildlife managers, all of which would add to the members' enjoyment of the recreation on IP property and lower the company's costs.

IP had already made substantial investments in experimental wildlife management programs and knew the potential for integrating wildlife management with timber programs. In 1957 the company established its 16,000-acre Southlands Experimental Forest near Bainbridge, Georgia. This forest served as a proving ground for management techniques that harmonize timber production and the needs of wildlife while earning profits from recreation. Exemplifying the innovative techniques pioneered at Southlands were experiments with prescribed burning.

Fire is an important tool in the management of southern pine forests. Because the pines are fire-resistant, periodic burning reduces competitive undergrowth and thereby enhances timber production. Prescribed burning also benefits wildlife by promoting the growth of browse essential to white-tailed deer and bobwhite quail. Prior to the Southlands burning projects, deer, turkey, quail, and rabbit populations in the experimental forest were low. By the early 1980s, however, prescribed burning had dramatically increased populations of these species. After visiting Southlands, outdoor writer Richard Starnes concluded, "Experiments with whitetails, turkey, quail, dove, rabbits, and a host of other game and nongame species are proving that it is practical—and profitable—to manage continuous-yield tree plantations in a way that ensures the healthy proliferation of wildlife."

Hunting Club Leases

Under Bourland's direction, IP launched its fee-based wildlife and recreation program in

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1983, emphasizing three sources for revenues: hunting club leases, daily-use permits, and seasonal family permits. By 1986, the program had made dramatic strides. Revenues from recreational sales in Arkansas, Louisiana, and Texas had tripled to $2 million, and corresponding profits were an impressive 25 percent of total profits in IP's mid-south region. Fourteen hundred hunting clubs had leased one million acres of IP lands, more than double the amount leased by the end of 1983. The results convinced the skeptics.

"Managed fee hunting programs are gaining acceptance among hunters seeking exclusivity, safer conditions, and abundant game," Bourland said. He pointed out that the hunting clubs are an integral part of wildlife management because they "can provide wildlife protection, control harvest pressure, and accomplish habitat improvements to a degree not generally possible through other arrangements." In addition, a new partnership, or "contract," between recreational users and the company was being formed among a growing number of clubs that gave new meaning to wildlife management. At a club's request, company biologists provided members with wildlife-management guidance, survey assistance, harvest analysis, and food-plot material. In return, club members restricted their hunting techniques, recorded harvests, and followed company-imposed restrictions on harvests. By 1986, new contracts had been adopted by nearly one-third of the clubs that leased IP land.

The company also began experimenting with other recreational packages. At the upper end of the scale, IP opened the 3,000-acre Big Oak Club in East Texas. In 1986, hunters at the club paid $200 per day for lodging and guides and for the opportunity to take one buck and two doe white-tailed deer. Farther down the price scale was the 1985 opening of the 4,000-acre San Patricio Bowhunting Area. Bowhunters using the area paid $200 per season or $100 for a three-day hunt and enjoyed a success rate of 61 percent. Services provided by the company included a walk-in cooler and campsites furnished with electricity, water, tables, grills, and bathroom facilities.

Most importantly, as revenues from IP's recreational program grew, regional forest managers began managing their forests differently. In 1988, speaking to congressional staff members in Big Sky, Montana, Bourland described the new behavior of the timber owners: "Because the status of wildlife affected the bottom line, the landowner bent over backwards to provide habitat for white-tailed deer, wild turkey, fox, squirrel, and bobwhite quail, as well as endangered bald eagles and red-cockaded woodpeckers." They left corridors of trees 100 yards wide between harvested areas through which wildlife could travel safely. They left clumps of trees uncut while younger stands next to them grew, thus creating greater age diversity. They reduced the size of cut areas and made their perimeters more irregular and therefore more attractive to a greater variety of wildlife. They did not harvest large strips of trees and shrubs along either side of streams, and they planted food plots.

These and other efforts have paid big dividends to wildlife as well as stockholders. Ten years after the inception of the program, game surveys showed that populations of deer, turkey, fox, quail, and ducks had increased substantially. Eastern wild turkey and white-tailed deer had exhibited the largest gains, increasing tenfold and fivefold, respectively. According to company biologists, the main reasons are better habitat and less hunting pressure. Nongame populations have also benefited. Company biologists carry out an assortment of projects to improve habitat for these species, from putting up bluebird boxes to protecting heron rookeries. Even though nongame species have no explicit market, hunters, campers, anglers, and hikers are willing to pay more for a diversified recreational experience. IP's biologists continue to explore other options that would provide additional revenue for nongame species.

The 1990s have been a time of change and continued success for the program. Bourland has left IP to form a flourishing business, providing wildlife and forest management consulting for private, nonindustrial (that is, small) timber owners in the South. In this new venture, Bourland is helping hundreds of pri-

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INTERNATIONAL PAPER

International Paper forestlands provide a scenic backdrop for canoeists. Ninety-six percent of the company's 6.2 million acres, stretching from Texas to Maine, are available to the public for recreational use.

vate forest owners benefit from the years of wildlife research carried out at IP. Meanwhile, IP's wildlife and recreation program continues to grow. Nearly two-thirds of the company's more than 6 million acres in the United States are now managed profitably for wildlife and recreation. Revenues from the program reached $10 million in 1990 and are expected to double rapidly. Thirty-five thousand hunting and recreational customers now use IP lands in Arkansas, Louisiana, and Texas, and another 25,000 pay to use IP lands elsewhere in the country. On the company's timber lands in northern Maine, for example, the public pays daily fees of $3 to $6 and seasonal fees of $15 to $90 for camping, hiking, fishing, and canoeing. In the Adirondack region of New York, people lease cabin sites, paying $700 to $1,000 per year.

The International Paper Company's wildlife and recreation program indicates a growing trend. In the South and the East, where most of the land base is privately owned, fee-based wildlife recreation is becoming firmly established. In addition, environmental entrepreneurs are coming up with new products and services to meet new markets. Texas ranches such as the King Ranch near Corpus Christi, the Fennessey Ranch near Baytown, and the Selah Ranch near San Antonio are providing nature hikes and bird-watching tours. In the West, where there is so much free access to public lands, it is tougher for the private landowners to compete, but the fee-recreation market is beginning to develop even there. Enviro-capitalists such as Tom Bourland are leading the way for new land management techniques.

This example illustrates how entrepreneurial skills can be successfully used to improve the environment. Entrepreneurial approaches that capitalize on profits in the marketplace offer an important alternative for producing environmental quality in a world where acrimony and tight budgets dominate most policy debates. □

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Regardless of Choice, Vote!

by Leonard E. Read

I have vowed never to support any organization which would take positions representing me, which positions I would not willingly (peacefully) stand personally responsible for. In short, I object to organizations that claim a consensus that does not exist—a false reporting of agreement growing out of committee action.

It is logical for anyone to inquire, "Well, what about support of and membership in one of the two major political parties? Would you go so far as to take part in neither of these? You would vote for the candidate of one or the other party, regardless of positions, wouldn't you?" These are good questions and deserve a careful answer, though I am not suggesting that anyone else adopt my view.

According to *The Columbia Encyclopedia,* "the existence of only two major parties, as in most English-speaking countries, presupposes general public agreement on constitutional questions and on the aims of government." This idea is fundamental to my thesis. Under such agreeable circumstances, each party keeps a check on the other, thus giving assurance that neither party will step out of the bounds that have been agreed upon.

Let it be re-emphasized that the two-party system (1) presupposes a general agreement on constitutional questions and the aims of government and (2) aims at, if it does not presuppose, honest candidates contending for office *within the framework of that constitution.* In this kind of political order, each office seeker is supposed to present fairly his own capabilities as related to the agreed-upon framework, voting being for the purpose of deciding which candidate is more competent for that limited role.

Clearly, the theory as originally conceived did not intend that the positions of candidates should be a response to voter opinion polls concerning the content or meaning of the constitution and the aims of government. If voters could thus reshape or reform the boundaries of government at will, there would be no need of candidates. Far less costly and more efficient would be the purchase of an electronic computer into which voter opinions and caprices would be continually fed; it could spew out altered constitutions and governmental purposes every second!

If there were "a general public agreement on constitutional questions and on the aims of government," and if candidates were vying with each other for office solely on their competency to perform within this framework, I would have no comment. But there is little contemporary agreement as to constitutional questions and the aims of government! Name a point that can now be presupposed. Both the questions and the aims are at sixes and sevens.

And as to candidates—with a few notable exceptions—they no longer contend with

Leonard E. Read established FEE in 1946 and served as its president until his death in 1983. This article is excerpted from Chapter 9 of Mr. Read's book Anything That's Peaceful. *It is the eleventh in a monthly series commemorating the 100th anniversary of Mr. Read's birth.*

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each other as to their competence to serve within a generally accepted framework but, instead:

(1) they compete to see which one can come up with the most popular alteration of the framework, and

(2) they compete to see which one can get himself in front of the most popular voter grab bag in order to stand four-square for some people's supposed right to other people's income.

The upshot of this political chaos is that voters are seldom given the chance to decide on the basis of competency but have only the choice of deciding between opportunists or, a better term, *trimmers.* This changed situation does, indeed, call for comments about political party membership and voting.

Despite the respectability of the two-party theory, its practice has "come a cropper." Today, trimming is so much in vogue that often a voter cannot cast a ballot except for one of two trimmers. Heard over and over again is the apology, "Well, the only choice I had was to vote for the lesser of two evils. I had to vote for one of them, didn't I?" A moral tragedy is implicit in this confession, as well as a political fallacy; in combination they must eventually lead to economic disaster.

I. The Moral Tragedy

It is morally tragic whenever a citizen's only choice is between two wrongdoers—that is, between two trimmers.

A trimmer, according to the dictionary, is one who changes his opinions and policies to suit the occasion. In contemporary political life, he is any candidate whose position on issues depends solely on what he thinks will have most voter appeal. He ignores the dictates of his higher conscience, trims his personal idea of what is morally right, tailors his stand to the popular fancy. Integrity, the accurate reflection in word and deed of that which is thought to be morally right, is sacrificed to expediency.

These are severe charges, and I do not wish to be misunderstood. One of countless personal experiences will help clarify what is meant: A candidate for Congress sat across the desk listening to my views about limited government. At the conclusion of an hour's discussion he remarked, "I am in thorough accord with your views; you are absolutely right. But I couldn't get elected on any such platform, so I shall represent myself as holding views other than these." He might as well have added, "I propose to bear false witness."

No doubt the candidate thought, on balance, that he was justified, that The Larger Good would be better served were he elected—regardless, of how untruthfully he represented his position—than were he to stand for his version of the truth and go down to defeat.

This candidate is "a mixed-up kid." His values are topsy-turvy, as the saying goes. In an egotism that has no parallel, he puts his election to office above honesty. Why, asks the responsible voter, should I endorse dishonesty by voting for such a candidate? He has, on his own say-so, forsworn virtue by insisting on bearing false witness. Does he think his ambition for office is right because he needs a job? Then let him seek employment where want of principle is less harmful to others. Or, is his notion of rightness based on how much the rest of us would benefit by having him as our representative? What? A person without moral scruple representing us in Congress! The role of the legislator is to secure our rights to life, liberty, and property—that is, to protect us against fraud, violence, predation, and misrepresentation (false witness). Would our candidate have us believe that "it takes a crook to catch a crook"?

Such righteousness or virtue as exists in the mind of man does not and cannot manifest itself in the absence of integrity—the honest, accurate reflection in deeds of one's beliefs. Without this virtue the other virtues must lie dormant and unused. What else remains? It is doubtful if anything contributes more to the diseased condition of society than the diminishing practice of integrity.

Those of us who attach this much importance to integrity must perforce construe trimming as evil. Therefore, when both candidates for public office are judged to be trimmers, the one who trims less than the other is often regarded as "the lesser of two evils." But, is he

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really? It must be conceded that there are gradations of wrongdoing: killing is worse than stealing, and perhaps stealing is worse than covetousness. At any rate, if wrongdoing is not comparative, then it is self-evident that the best of us are just as evil as the worst of us; for man is fallible, all men!

Degrees of Evil

While categories of wrongdoing are comparative, it does not follow that wrong deeds within any given category of evil are comparative. For instance, it is murder whether one man is slain, or two. It is stealing whether the amount is ten cents or a thousand dollars. And, a lie is a lie whether told to one person or to a million. "Thou shalt not kill"; "Thou shalt not steal"; "Thou shalt not bear false witness" are derived from principles. Principles do not permit of compromise; they are either adhered to or surrendered.

Is trimming comparative? Can one trimmer be less at fault than another trimmer? Does the *quantity* of trimming have anything whatsoever to do with the matter? Or, rather, is this not a question of *quality* or character? To trim is to ignore the dictates of higher conscience; it is to take flight from integrity. Is not the candidate who will trim once for one vote likely to trim twice for more votes? Does he not demonstrate by any single act of trimming, regardless of how minor, that he stands ready to abandon the dictates of conscience for the place he seeks in the political sun? Does not the extent or quantity of trimming merely reflect a judgment as to how much trimming is expedient?

If the only question at issue is whether a candidate will trim at all, then trimming is not comparative; thus, it would be incorrect to report, "I cast my ballot for the lesser of two evils." Accuracy would require, "I felt there was no choice except to cast a ballot for one of two men, both of whom have sacrificed integrity for the hope of votes."

We must not, however, heap all our condemnation on candidates who trim. There would be no such candidates were it not for voters who trim. Actually, when we find only trimmers to vote for, most of us are getting what we deserve. The trimmers who succeed in offering themselves as candidates are, by and large, mere reflections of irresponsible citizenship—that is, of neglected thinking, study, education, vigilance. Candidates who trim and voters who trim are each cause and each effect; they feed on each other. *When the worst get on top it is because there are enough of the worst among us to put them there.*

To repeat, when one must choose between men who forsake integrity, the situation is tragic, and there is little relief at the polling level except as candidates of integrity may be encouraged by voters of integrity. Impractical idealism? Of course not! Read Edmund Burke, one of the great statesmen of all time, addressing his constituency:

> But his [the candidate's] unbiased opinion, his mature judgment, his enlightened conscience, he ought not to sacrifice to you, to any man, or to any set of men living. These he does not derive from your pleasure—no, nor from the law and the Constitution. They are a trust from Providence, for the abuse of which he is deeply answerable. Your representative owes you, not his industry only, but his judgment; and he betrays instead of serving you, if he sacrifices it to your opinion.

II. The Political Fallacy

Is it fallacious to believe that responsible citizenship requires casting a ballot for one or the other of two candidates, *regardless of how far the candidates have departed from moral rectitude?*

Before trying to arrive at an answer, let us reflect on the reason why the so-called duty of casting a ballot, regardless of circumstance, is so rarely questioned. Quite obviously, the duty to vote is one of those sanctified institutions, such as motherhood, which is beyond criticism. The obligation to vote at any and all elections, whatever the issues or personalities, is equated with responsible citizenship. Voting is deeply embedded in the democratic mores as a duty, and one does not affront the mores without the risk of scorn. To do so is to "raise the dead": it is to resurrect questions

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that have been settled once and for all; it is to throw doubt on custom, tradition, orthodoxy, the folkways!

Yet any person who is conscious of our rapid drift toward the omnipotent state can hardly escape the suspicion that there may be a fault in our habitual way of looking at things. If the suspicion be correct, then it would be fatal never to examine custom. So, let us bring the sanctity of voting into the open and take a hard look at it, in a spirit of inquiry rather than advocacy.

Now for the hard look: Where is the American who will argue that responsible citizenship would require casting a ballot if a Hitler and a Stalin were the opposing candidates? "Ah," some will complain, "you carry the example to an absurdity." Very well, let us move closer to home and our own experience.

Government in the U.S.A. has been pushed far beyond its proper sphere. The Marxian tenet, "from each according to ability, to each according to need," backed by the armed force of the state, has become established policy. This is partly rationalized by something called "the new economics." Within this kind of political framework, it is to be expected that one candidate will stand for the coercive expropriation of the earned income of all citizens, giving the funds thus gathered to those in groups A, B, and C. Nor need we be surprised that his opponent differs from him only in advocating that the loot be given to those in groups X, Y, and Z. Does responsible citizenship require casting a ballot for either of these political plunderers? The citizen has no significant moral choice but only an immoral choice in the event he has joined the unholy alliance himself and thinks that one of the candidates will deliver some of the largess to him or to a group he favors. In the latter case, the problem is not one of responsible citizenship but of irresponsible looting.

The Duty to Vote

Does responsible citizenship require voting for irresponsible candidates? To ballot in favor of irresponsible candidates as though it were one's duty is to misconstrue the meaning of duty. To cast a ballot for a trimmer, because no man of integrity is offering himself, does as much as one can with a ballot to encourage other trimmers to run for office. Can anyone conceive of any element of protest in such balloting? To vote for a trimmer goes further: it would seem to urge, as strongly as one can at the polls, that men of integrity not offer themselves as candidates.

What would happen if we adopted as a criterion: *Never vote for a trimmer!* Conceding a generous liberality in defining trimmers, millions of us would not cast ballots. Would the end result of this substantial, nonviolent protest, this large-scale demonstration of "voting by turning our backs," compound our problem? It is difficult to imagine how it could. For a while we would continue to get what we now have: a high percentage of trimmers and plunderers in public office, men who promise privileges in exchange for ballots—and freedom. In time, however, this silent but eloquent refusal to participate might conceivably improve the situation. Men of integrity and high moral quality—statesmen—might show forth and, if so, we could add their numbers to the few now in evidence.

Would a return to integrity by itself solve our problem? No, for many men of integrity do not understand freedom; or, if they do, are not devoted to it. But it is only among men of integrity that any solution can *begin* to take shape. Such men, at least, will do the right as they see the right; they tend to be teachable. Trimmers and plunderers, on the other hand, are the enemies of morality and freedom by definition; their motivations are below the level of principles; they cannot see beyond the emoluments of office.

Here is a thought to weigh: If respect for a candidate's integrity were widely adopted as a criterion for casting a ballot, millions of us, as matters now stand, would not cast ballots. Yet, in a very practical sense, would not those of us who protest in this manner be voting? Certainly, we would be counted among that growing number who, by our conscious and deliberate inaction, proclaim that we have no party. What other choice have we at the polling level? Would not this encourage men of statesmanlike qualities to offer themselves in candidacy? □

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Asset Forfeiture Run Amok

Seventy-year-old Joseph Puertas and his family will never forget one cold night in December 1997 when police and drug-sniffing dogs came calling at the doors of both his home and his business and, at the same time, those of his three sons as well.

Based on the word of an "informant," who was a self-confessed addict with two prior felony convictions, the Oakland County, Michigan, police searched all the buildings for evidence of drug dealing. They found no drugs, no drug paraphernalia, no records of drug transactions, and no other evidence of drug dealing. They did find one small plastic bag of powder, which on examination, turned out to be Slim Fast.

But the search wasn't exactly fruitless, at least for the searchers. The Oakland County prosecutor's office may wind up more than $5 million richer: $3.2 million from selling the Puertas family's bowling alley, which the police seized, plus $1.9 million in cash, jewelry, and coins. A pretty good haul for a few hours' hard work by the boys in blue.

The property seizures that December night, incidentally, did not lead to any charges or convictions. One charge was filed against Joseph Puertas based only on the dubious word of the informant—who, incidentally, may have framed the family to secure leniency on the felony charges he now faces. In any event, most of the property seized does not even belong to Joseph Puertas, but to other family members.

"They arrest my father and take from us what we have spent years working for, based on what some crackhead tells them," Steve Puertas told the *Detroit Free Press*. "You tell me that's justice?"

The newspaper's account of how the authorities defended their action, and the response of the Puertas family's attorney, James Burdick, is instructive:

"Why would they forgo thousands of dollars of interest they could have made if they had put their money in the bank?" asked prosecutor James Halushka, director of warrants and investigations for the Oakland County Prosecutor's Office. "If this isn't dirty money, why didn't they put it in the bank?"

Burdick's response: "Show me the law that says you have to put your money in a bank."

Seizing property from the innocent—or at least from people who haven't been convicted of a crime—is not always drug-related. Consider the case of John and Tina Bennis of Royal Oak, Michigan.

On October 3, 1988, police found John Bennis engaging a prostitute in the front seat of his car. Bennis was convicted of indecency and fined $250. The police then obtained a civil court order to seize Bennis's car as a "public nuisance."

Tina Bennis, who as John's innocent wife endured the troubles and embarrassment that attended her husband's indiscretion, was half-owner of the vehicle. She had helped pay for

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the car with her babysitting income and used it to take the couple's five children to and from school. But the authorities refused to recognize that she had any interest in the vehicle. In a 1996 decision with far-reaching implications, the U.S. Supreme Court upheld the authority of the government to punish Tina Bennis for the actions of her husband by keeping the car.

These cases involve an alarming practice known as "civil-asset forfeiture." Not unique to Michigan, they are occurring in every state all across America with disturbing frequency. In civil-asset forfeiture cases, the government may do little more than meet the most minimal threshold for alleging that criminal activity has taken place. No criminal charges need to be filed, and no convictions need to be gained for law enforcement authorities to seize and keep the property of citizens. Indeed, even an acquittal on any criminal charges to which seized property relates will not necessarily immunize an individual from a forfeiture proceeding. If the owner wishes to recover his property, he has the burden of showing that it was not used in the commission of a crime.

Enacted to help the government nail "drug kingpins" and other big-time lawbreakers, forfeiture laws often scoop up the homes, cars, and cash of ordinary law-abiding citizens. The police usually oppose any curbs on the practice because they normally get the cash or the profits from the sale of seized property.

Civil-asset forfeiture operates on the principle that the *property*, not the individual, commits the crime. This legal fiction allows the government to "punish" property, leaving the owners themselves without the rights normally available to accused persons. But the very notion does violence to these pillars of law in a free and civilized society: *people* commit crimes, inanimate property does not, and people are innocent until they are proven guilty.

America's Founders understood the critical importance of property rights in preserving liberty. "No person shall . . . be deprived of life, liberty, or property without due process of law"—so says the Fifth Amendment to the U.S. Constitution. James Madison noted that "Government is instituted to protect property of every sort. . . . This being the end of government, that alone is a *just* government which impartially secures to every man, whatever is his own." Without a doubt, Madison and his colleagues, were they to witness property seizures under today's civil asset forfeiture laws, would decry the practice as reminiscent of the very tyrannies they and others once pledged their "lives, fortunes and sacred honor" to prevent.

Ending the government's senseless and counterproductive war on drugs would go a long way to stop the majority of today's most offensive forfeitures, but one does not have to be in favor of drug legalization to see the need for an array of legal reforms. In a recent study done for the Mackinac Center for Public Policy, Donald Kochan suggests:

- Enacting protections for the innocent. Language in forfeiture statutes should be strengthened to ensure that property owners who have not participated or acquiesced in a crime committed with their property are not punished with forfeiture.

- Shifting the burden of proof from property owners to the government. Governments at all levels should be required to prove that disputed property is in fact connected to illegal activity before it can be seized.

- Removing financial incentives for law-enforcement agencies to employ asset forfeiture. The cops shouldn't keep what they swipe.

John Adams advised that "Property is surely a right of mankind as real as liberty." The innocent victims of forfeiture-laws-run-amok can certainly attest to the fact that the seizure of property is equivalent to the loss of liberty. The rest of us ignore their plight at our own peril. □

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THE FREEMAN
Ideas On Liberty

A New Monetary Universe

by James A. Dorn

Electronic money (e-money) offers the possibility of privatizing the currency and making government fiat money disappear. Competition and falling processing costs will prompt e-money issuers to pay interest to users, and as people choose to hold that money rather than non-interest-bearing paper money issued by central banks, there will be a radical change in economic affairs.

Even central bankers are forecasting the demise of paper currency. Jerry L. Jordan, president of the Federal Reserve Bank of Cleveland, predicts that "Just as fiat money replaced specie-backed paper currencies, electronically initiated debits and credits will become the dominant payment modes, creating the potential for private money to compete with government-issued currencies."[1] And University of Georgia economist Lawrence H. White forecasts, "When commercial on-line networks and Internet sites begin offering offshore banking services, with zero or very small fees for transferring funds, an exodus of retail banking business will begin from the regulated onshore sector to the untaxed and unregulated offshore sector."[2]

The transition from the old monetary universe, with government at its center, to a new monetary universe, with the private market at its center, will be a slow process of evolution rather than revolution.[3] Because of habit and the network effects of paper currency, it will take time for people to adjust to new ideas and new technology and to accept digital cash (in the form of portable "smart cards" as well as Internet accounts) as a new medium of exchange.[4] Thus, the current monetary system will not disappear overnight.

Transition to a New Monetary Universe

The convenience of e-money, its anonymity, and its positive yield will make it increasingly attractive as a medium of exchange in the information age. So, as banks find ways to further reduce their reserves and clearing balances at the Federal Reserve, the net effect will be to reduce the demand for central bank money (the monetary base). The Fed will then have to reduce the supply of base money to prevent inflation. In the process, the Fed will suffer losses. (Seigniorage, by which the Fed currently profits through issuing currency for interest-bearing government bonds, would become negative.) If the public and banks continue to move out of non-interest-bearing government fiat money (in the form of currency in circulation and deposits at the Fed) and into e-money, the central bank will eventually go out of business.[5]

The market will fill the void and provide a new monetary standard as people demand sound money. Private entrepreneurs will have an incentive to maintain the value of their cur-

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rencies or be forced out of business; consumers will unload bad monies and switch to monies with reliable purchasing power.[6] A market-driven monetary regime will then emerge in which the monetary unit would be fixed in value by making it convertible into a basket of commodities or, more likely, into mutual fund shares.[7] Market forces will ensure that the supply of money will respond to changes in demand without experiencing the disrupting effects of monetary disequilibrium that occur under the current fiat money regime, in which money has no guaranteed value.[8]

The Flexibility to Experiment

In the choice of monetary institutions, F. A. Hayek wrote, "selection by evolution is prevented by government monopolies that make competitive experimentation impossible."[9] Thus, the key to whether a new monetary regime evolves is competition—that is, the freedom to experiment. Will private, profit-seeking entrepreneurs, operating within the spontaneous market process, be allowed to discover a new monetary universe or will government planners and regulators attempt to block that process by protecting the status quo? Ultimately, the answer to that question may be that the forces of technology and competition will make it impossible to prevent private-sector suppliers of e-money from breaking the government's monopoly on currency.

Financial innovation depends on the freedom to fail, as well as the right to profit from success. Markets are driven by individuals who are willing to take risks in search of new opportunities and profit. In the process, privately sanctioned informal rules often emerge that later become codified and enforced by government; the market typically leads the process of innovation, and government follows. Misguided government intervention would cause more problems than it cures. If overzealous regulators restrict experimentation and make the emerging electronic marketplace too costly, they will severely hamper the development of e-money.

How the Congress, Federal Reserve, and Treasury, in particular, view the transition to electronic cash and commerce will shape the future of the electronic payments system. A laissez-faire attitude will foster innovation; a protectionist attitude will mean that special interests will determine the pace of innovation. The challenge for government will be to provide a legal framework that safeguards property rights and expands markets so that wealth is created rather than destroyed. As Federal Reserve Board chairman Alan Greenspan has noted, "If we wish to foster financial innovation, we must be careful not to impose rules that inhibit it. . . . [T]he private sector will need the flexibility to experiment, without broad interference by the government."[10]

Private entrepreneurs, such as David Chaum of DigiCash, are already developing the technology needed to ensure privacy and security in the electronic payments system. Chaum, a pioneer in developing blind-signature technology (the use of encryption to generate secure digital signatures), is confident that the new technology will allow electronic cash to come very close to having the attributes of paper currency without the costs. Moreover, that technology will allow users of e-cash to "retroactively and irrefutably reveal the recipient of the funds." Thus, crimes associated with the use of paper currency—such as extortion and bribery—"are no more likely than they are with checks today." His goal is to create "a payments system that can be widely adopted and that will stimulate economic growth . . . and act as a springboard for increasing individual freedom." Chaum believes that goal is achievable once "consumers realize that the use of electronic payments media does not have to compromise their privacy, but in fact can empower them to protect their own interests."[11]

Monetary Freedom and Individual Sovereignty

In the new monetary universe, the individual—not the state—will stand at the center. Market-driven money, not politicized government fiat money, will be the standard of value. Bill Frezza, president of Wireless Computing

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Associates, envisions an enlarged private space in which "sovereign individuals will have the tools to construct a practical realization of laissez-faire capitalism." At the center of that space, "will be new monetary institutions that must inherently rest on the consent of the participants."[12] In the new monetary universe, people will benefit from greater competition, more information, and more freedom.

The danger, of course, is that government may try to stifle competition, control information, and constrain freedom. Special-interest groups that benefit from a paper-based monetary system should not be allowed to maintain what Milton Friedman has called the "tyranny of the status quo." The challenge is to develop an institutional framework that provides trans-

3. Ibid., pp. 15–16.

4. Lawrence H. White, "Thoughts on the Economics of 'Digital Currency'," *Extropy*, 2nd–3rd Quarter 1995, p. 18.

5. A more detailed scenario of this transition process is found in Kevin Dowd, "Monetary Policy in the 21st Century: An Impossible Task?" *Cato Journal*, Winter 1998, pp. 327–31.

6. For a fuller discussion of why private enterprise will produce money of superior purchasing power, see F. A. Hayek, "Toward a Free-Market Monetary System," in James A. Dorn and Anna J. Schwartz, eds., *The Search for Stable Money* (Chicago: University of Chicago Press, 1987), p. 383. Also, more generally, see Hayek, *Denationalisation of Money—The Argument Refined*, 2d (extended) ed., Hobart Paper 70 (London: Institute of Economic Affairs, 1978).

7. In this "defined-value" monetary regime, the monetary unit would be defined by a basket of goods and services. Banknotes and bank accounts denominated in the unit would be maintained at their defined values by redeemability in equivalent amounts of some convenient redemption medium, perhaps mutual fund shares. Kevin Dowd has proposed a convertibility rule that is designed "to achieve price stability by pegging the prices of index-based financial derivatives." See Dowd, "Monetary Policy," p. 330, especially footnote 6.

8. For an excellent discussion of how to avoid monetary disequilibrium, see part four of Leland B. Yeager, *The Fluttering Veil: Essays on Monetary Disequilibrium* (Indianapolis: Liberty Fund, 1997), edited and with an introduction by George Selgin. Also see F. X. Browne and David Cronin, "Payment Technologies, Financial Innovation, and Laissez-Faire Banking: A Further Discussion of the

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THE FREEMAN
Ideas On Liberty

Does the Internet Prove the Need for Government Investment?

by Andrew P. Morriss

Fans of tax-funded investment often cite the Internet as an example of the good that government can do. Sure, they say, the Net now has uncountable millions of components, from Web sites to computer networks large and small. But if it hadn't been for those first critical investments by the government, we wouldn't have the Internet today. Politicians from Vice President Al Gore to Speaker Newt Gingrich now call for more such investments by the government—and the taxes to fund them. We must find and identify promising new technologies and invest in them to build tomorrow's information infrastructure, they tell us, a task too important to be left to private enterprise.

The actual history of the Internet suggests that this is far from accurate. The Internet today bears little resemblance either to what the government wanted to build or to what it actually built. The innovations in networking that produced today's Net occurred as much *despite* government funding as because of it. If anything, therefore, the Internet represents the success of spontaneous ordering over central planning, not the successful design of a new technology by the state.

What Is the Internet?

Examining the strength of the statist claim that government investment created the Internet requires thinking carefully about exactly what the Internet is. In a 1968 paper titled "The Computer as a Communication Device," two pioneering computer scientists, J.S.R. Licklider and Robert Taylor, set out the principles that continue to define the Internet today. According to Michael and Ronda Hauben, the principles consist of these ideas: "1. Communication is defined as an interactive creative process. 2. Response times need to be short to make the 'conversation' free and easy. 3. Larger networks form out of smaller regional networks. 4. Communities form out of affinity and common interests."[1] Perhaps most striking about this definition is its similarity to the description of an open society built around free markets.

Implementing this vision requires connections between computers. The hardware part of the Internet consists of millions of interconnections between computer systems across the world. My office computer, for example, is connected by a fiber optic cable to a server on my university campus. The server in turn is connected to the telecommunications lines owned by many companies. Those lines eventually lead, by an unknowable number of paths, to *Freeman* editor Sheldon Richman's computer.

The software part of the Internet distinguishes its networking capabilities from that of the telephone system. Those capabilities enabled me to make use of these physical connections to submit this article by e-mail. My computer's mail program chopped the

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article into many small pieces, or packets, addressed them to Richman care of his Internet service provider (ISP), and sent them out along many different paths using a technique called "packet-switching." When the pieces reached the ISP, they were reassembled for downloading, making the document legible on his computer screen. The transmission of information in these small packets is a key feature of the Internet; it is what enables the Net to transmit much more information than the conventional telephone network, which requires dedication of a circuit between the telephones on each end for the duration of the call. Transmitting information over the Internet allows multiple uses of the same connection, mixing packets of information from my e-mail with yours, for example, and then sorting them out at the appropriate points. The "pipeline" between two points can therefore be kept continuously full, with no wasted time for pauses in conversations or while one caller answers the doorbell in the middle of a call.

The Internet is thus a complex system—a mixture of hardware and software and millions of computers of every conceivable make and design running different operating systems. And thanks to voluntary and mutual coordination by millions of people, as in a free market, they all talk to each other to provide us with an unimaginable variety of information and services, commercial and free. It is a network of networks.

Today's Internet is the embodiment of a spontaneous order in many ways. No agency or board controls it. No central planner decides how it will operate. It ignores national borders. It has changed the world.

Yet a few years ago, little of what we know today as the Internet existed: no bookstores, no Web pages, little public access beyond academic institutions. Before the Internet, there was ARPANET—the Advanced Research Projects Agency Network—a U.S. Department of Defense (DOD) network that is often described as the forerunner of today's Internet. The ARPANET connection is thus the source of the "we wouldn't have it without the government" story.

The Birth of ARPANET

Concern over secure military communications in the early 1960s, sparked in part by an act of sabotage against three Defense Department microwave towers in Utah in 1961, led the U.S. military to commission a series of studies by the RAND Corporation. DOD wanted a decentralized communications network that could survive a nuclear attack and permit the United States to launch missiles in retaliation. The RAND work included a description of the theoretical basis for a packet-switching network. Packet-switching would permit messages to be routed around damaged parts of the network. RAND was not interested in implementing the reports, however, and nothing was done with them for several years. DOD continued to fund research; as a result, much of the pioneering work on networking was either classified or in unpublished DOD reports and so unavailable outside the government.[2]

Also during the 1960s, new operating systems allowed mainframe computers to handle more than one user at once through "time-sharing" methods. As computers increased in speed and flexibility, these operating systems allowed the huge costs of hardware to be spread over more users. Differences in capabilities among the various types of computers at different facilities produced interest in communicating between machines as well, in order to allow researchers to avoid duplicating hardware. Networking thus naturally followed from time-sharing.[3] The Defense Department was particularly interested in these developments because of its extensive investment in computers at universities across the United States, and it continued to fund networking research, largely through the Information Processing Techniques Office (IPTO).

Far from setting out to design the Internet at the command of bureaucrats, researchers did much of the early work as "extras" on existing contracts, diverting resources to unofficial projects.[4] Indeed, the first director of IPTO has been described as a "'Johnny Appleseed' with a mission" to promote networking, rather than as someone merely responding to his superiors' goals.[5] More than funding was diverted to these projects. IPTO also managed

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to hire whatever private researchers the director wanted.[6]

Even when the official decision was made to set up a network connecting research sites, no one knew what uses the network would be put to. For example, Henry Edward Hardy writes that "The popularity of electronic mail on the early ARPANET was unanticipated by its designers."[7] The informal "Network Working Group" shaped the network. But decisions were made not by the Defense Department or by university bureaucracies; rather they were made by free-wheeling technical working groups that formed spontaneously. "What began [at the early meeting] was the creation of a community which cooperated more-or-less harmoniously for over 15 years," Peter Salus writes.[8]

While groundwork for the ARPANET was being laid, few outside the technical groups had much enthusiasm for the project. Many were skeptical about packet-switching. The project also struggled with "a feeling that with the government involved it would be five years late and nothing would work."[9] Only after a successful demonstration at a 1972 computer conference did much enthusiasm appear. (ARPANET was not the only government-funded networking experiment during the 1960s and 1970s. The French, German, British, and Japanese governments also funded network development. None was particularly successful and none produced anything like the Internet. American technical superiority doesn't explain the success of ARPANET; other Defense Department networking efforts failed miserably.[10])

Thus the story of ARPANET is fascinating but it is not the commonly accepted myth that government investment produced the Internet. Far from being centrally planned, ARPANET grew up as the result of the successful capture of agency (and private) resources by individuals pursuing their own academic interests. The availability of no-strings-attached federal defense dollars undoubtedly made it easier for the early networking pioneers to concentrate on the technical details of their work. Given the intensity of their interest in the subject, however, subsidies were hardly required. Other money would surely have been found.

Why Was There No "Private ARPANET"?

Government activity generally "crowds out" private activity by absorbing resources that could be used elsewhere. Computer networking is no exception. Not only did the government directly seize resources through taxation and lock up knowledge in classified documents, it also lured many of the best computer scientists to work on its projects, slowing private-sector activity.

Private networks were attempted, but they failed. Setting up a network required permission from the Federal Communications Commission, and existing communications companies like Western Union fought the creation of new networks. Even when a private packet-switching network, Telenet, began operation, "many millions in legal expenses" were required to fight the regulatory battle prompted by RCA, ITT, AT&T, and Western Union. This kept Telenet from making profits for years.[11] Regulatory barriers to entry, not a lack of entrepreneurial activity, slowed the efforts to build private networks.

Despite these obstacles, a private network among universities, USENET, sprang up. It resembled today's Internet much more than ARPANET did. USENET developed because the Defense Department limited ARPANET to a relatively small number of sites. People at other sites wanted a network too, and USENET quickly surpassed ARPANET in usefulness because it lacked the restrictions DOD money imposed on ARPANET. (USENET still exists; it is a collection of newsgroups devoted to every subject imaginable.)

ARPANET Was Not the Internet

The Internet had its genesis within ARPANET. The protocols, or common language that all computers can use to communicate with each other, were developed by ARPANET people. In 1979 the government's Advanced Research Projects Agency established the Internet Configuration Control Board. Both ARPANET and the Internet are packet-switched networks. But there are many profound differences. Indeed, the Internet

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today is so vast and complex as to be virtually impossible to describe accurately. It is a highly decentralized open-ended process that is not governed in any literal sense. (The Internet Society, a nongovernment, nonprofit organization, was formed in 1992 to "maintain and extend the development and availability of the Internet and its associated technologies and applications.") There are several defining characteristics that make the Internet what it is and sharply differentiate it from ARPANET.

- Its constant and rapid growth: There are hundreds of thousands, if not millions, of connections on the Internet depending on how one defines "connection." ARPANET, in contrast, grew slowly. In 1969 there were just four host computers connected. By January 1976 there were just 63. ARPANET's limited scope was due to its restriction to sites with DOD funding.[12]
- Its freedom with respect to content: It is nearly impossible to control how individuals use the Internet. Because it was built with government funds, ARPANET users faced a number of restrictions on their use of the network. Commercial use, for example, was banned. Even one of the most popular uses, newsgroups, quickly ran into censorship problems. Although the first newsgroups concerned primarily technical issues about the network, users quickly began to establish groups concerning other subjects of interest. When several users proposed a newsgroup dealing with recreational drugs, those in control of the network rejected it as too controversial. (Drugs weren't the only subject that was rejected; a proposal for a newsgroup called "gourmand" was also turned down because the creator refused to change the name to "recipes.")
- Its quick and spontaneous evolution of standards: For example, the HTML language for producing web pages is quite recent but is now used throughout the world. The early network protocols developed by the hackers and graduate students who built the initial ARPANET software evolved into a system whose popularity prevented an international standards body from centrally planning a new system (OSI), although a number of government-sponsored networks attempted to impose it.[13]
- Its obliviousness to geography and borders. *Wired* magazine recently sent Internet pioneer (and Grateful Dead lyricist) John Perry Barlow across Africa to test network accessibility in remote corners of the continent; he found an astounding degree of connectivity already in existence. Connecting to the world outside DOD-funded sites was a problem for ARPANET users. Even sending e-mail across a university campus from a non-ARPANET site to an ARPANET computer often required routing messages across continents.

The international connections that are such an important part of the Internet today were also a struggle for the early ARPANET pioneers. Once the network expanded beyond a few experimental connections to universities abroad, international standards bodies dominated by representatives of government postal and telephone monopolies began to interfere with the protocol standards.

The Internet after ARPA

ARPANET and its successors were eventually shut down beginning in 1990 and network traffic shifted to a mix of private and public transmission lines by 1995, a period of unparalleled growth in both network usage and technology. The ARPANET experience did contribute significantly to the development of the Internet in a number of important ways. The experience with networking gained from running ARPANET, for example, helped thousands of computer scientists make advances that benefit us all today. Even more important, the drawbacks to a government network prompted ARPANET users to develop techniques for outwitting government controllers. That experience helped create the Internet. As Jim Gilmore, an important figure in evading the early attempts at censorship told Peter Salus, "when faced with obnoxiously centralized control over something that ought to be free and/or distributed, I look for a low overhead way around that increases freedom in general."[14]

There have been other sources of technical innovation as well, however, and they deserve

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as much credit as the Defense Department, if not more, for the Internet's capabilities today. A recent article in *Wired* magazine attributed advances in credit-card processing and video-streaming technology to a company selling pornography on line. Those techniques are now used by mainstream vendors as well.[15]

Unlike the mythical Internet that sprang forth from the ARPANET, the real Internet grew out of a spontaneous ordering process of the interactions of millions of individual users. The uses we make of the Internet were unimaginable to the researchers and scientists who created the networking protocols and hardware advances we rely on today. Far from being the result of the government's "strategic" investment in the original Defense Department networks, today's Internet developed at most accidentally from and often in spite of those investments. The explosive growth in commerce, for example, became possible only when the government's ban on commercial use of the networks it financed was lifted.

Moreover, the "strategic" nature of the early investment in networking is a myth. No one consciously created the Internet. While an international network of networks undoubtedly would look different today had ARPANET never existed, there is also little doubt that packet-switching and e-mail would have evolved anyway. Dedicated, motivated people with a need to communicate—for commercial and noncommercial purposes—would have surely seen to it. □

1. Michael Hauben and Ronda Hauben, *Netizens: On the History and Impact of Usenet and the Internet* (Los Alamitos, Calif.: IEEE Computer Society, 1997). The original paper is available at http://memex.org/licklider.html.
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4. Peter Salus, *Casting the Net: From ARPANET to INTERNET and beyond . . .* (Reading, Mass.: Addison Wesley Publishing Company, 1995), p. 25.
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7. Henry Edward Hardy, "The History of the Net," master's thesis, Grand Valley State University, September 28, 1993; at http://info.isoc.org/guest/zakon/Internet/History/History_of_the_Net.html.
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13. Salus, p. 123.
14. Ibid., p. 143.
15. Frank Rose, "Sex Sells," *Wired*, December 1997.

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Ideas On Liberty

Opening Pandora's Box

by Dan Fylstra

Last year, Netscape and several other PC industry companies appealed to our government to help them in their fight against Microsoft, which they felt was using its market power with Windows to gain an unfair advantage in the browser wars. Our federal and state governments have responded, and the results are everywhere in the daily news. I'd like to comment, not about Netscape or Microsoft, but about the politicization of our industry, what it means for our future, and what fundamental choices we can make going forward.

Somehow, things are not working out quite the way we expected. Now, in countless trade-press articles, columns, and editorials, people are asking: Should the government be involved? Will it do the right thing—whatever that is? And how will it impact us? Have we opened Pandora's box?

My answer to that last question is yes. We've opened Pandora's box—and it will prove impossible to close it. Our industry is being politicized. Henceforth, it won't be enough to design and build great products, and sell them at attractive prices. We'll also have to compete in the political sphere. And that will take time and money, which will be siphoned off from product development and marketing. We'll have to worry about whether we have enough influence in Washington, and in our state capitals. Have we hired the right lobbyists, donated to the right PACs, hobnobbed with the right politicians? Will we get our share of any government largess, and can we sneak in our special exemption from the latest tax or regulation?

There will be a new pecking order, defined by the amount of political influence enjoyed by various companies, trade associations, and other groups. And who is likely to come out on top of this new pecking order? The start-ups with the hottest new technology, or the established companies who've had the time to develop their political connections? Let's be blunt: it's pretty obvious that in today's White House and Congress, influence can be bought, and the price tag isn't all that high by our industry's standards. If a night in the Lincoln bedroom goes for $50,000 and a seat on a Commerce Department trade mission is just $100,000, then established leaders in the PC industry ought to be able to afford plenty of influence. As for the small and medium-sized companies—well, if you can't afford to pay, you can't afford to play.

Who Among Us Will Have the Most Influence?

And who can afford the most influence? Which company is responding to the pressure

Dan Fylstra has been involved in the PC industry since its inception. He was founding associate editor of BYTE Magazine *in 1975, and founder of VisiCorp in 1979. He is currently president of the PC software vendor Frontline Systems, Inc., and can be reached at danfylstra@hotmail.com. This is excerpted from a longer "open letter" distributed on the Internet.*

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brought upon it by drastically stepping up its lobbying efforts and political contributions? Microsoft, of course. Bill Gates is no dummy, and he's said it quite explicitly: he used to think that all he had to do was design and build great products. Now he realizes that attitude was "naïve." The folks who hate Microsoft, the 800-pound gorilla in a relatively free market, should be worrying about the future Microsoft, the gorilla with so much political influence—so many senators and congressmen in its back pocket—that it's practically untouchable. No, this won't happen next month or next quarter, but what about four years from now, given our politics today?

We've worried about the market power of a few companies like Microsoft, but we haven't anticipated how the true coercive power of government might be used for or against us. After all, you don't have to buy Windows 98, and many people won't. But you do have to pay your taxes, or go to jail, to finance things like the federal Market Promotion Program, which pays for McDonald's hamburger ads overseas today, and—who knows?—might pay for Microsoft's browser ads overseas tomorrow.

Most of us cling to the notion, or at least the hope, that the Justice Department or the state attorneys general will somehow act intelligently in the public interest, and things will turn out okay. We've never examined public choice theory, which predicts that in the public sector, as in the private sector, key players will pursue their own self-interest, not the broad public interest. We need to recognize the state attorneys general for what they are: political entrepreneurs who are simply riding the anti-Microsoft wave for all it's worth, seeking to advance their own careers. The results for consumers or for our industry are beside the point, as long as we are not that politically influential. Indeed, public choice theory predicts that a political system like ours will transfer wealth from the politically unorganized to the politically influential. The ideal outcome, from the politicians' viewpoint, is that we all become supplicants, on an ongoing basis, fighting among ourselves for the favors that only they can hand out.

What Are Our Choices?

Pandora's box is open. The impact of politics on our livelihoods is growing every day, and we don't know what to do about it. Most of us would rather avoid thinking about or spending time on politics; we'd rather be creating new technology, and satisfying more customer wants and needs. Many of us, if asked, would echo the classic cry: laissez faire—leave us alone! But the politicians won't leave us alone. Because of our relative lack of sophistication and lack of involvement in politics, we are on the defensive. We're likely to end up on the short end of any compromise—whether it's about strong encryption, Internet access and freedom of speech, electronic commerce and sales tax, you name it. So, if Pandora's box is open, what are our choices? Continuing to ignore politics is not really an option, because politics has arrived at our door. We can, of course, accept the politicization of our industry—as some have already done—and become supplicants. We can become active in "mainstream" politics, in either the Democratic or the Republican Party (is there any difference?), trying to move the politicians in a sensible direction, and hope for the best.

Or, we can apply some lessons from our own experience and try to gain leverage by investing in a start-up. Not another high-tech company, but a political start-up that is capable of challenging the status quo. I'm thinking broadly of the libertarian movement. . . .

It's no secret that libertarian ideas are popular on the Internet, or that they are showing up across our politics and culture with increasing frequency. But what practical difference would it make if the high-tech community were to embrace the libertarian movement in a big way? I believe that if enough of us made this decision, it would fundamentally alter the future, both for our industry and for American politics. For the high-tech community, an investment of time, energy, and money stands to earn a far bigger share of the "libertarian start-up" than we will ever gain from the established political parties. Instead of being absorbed into the enormous pool of current political interest groups, we could

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play a major role from the beginning. It is already true that the libertarians, on average, have a much deeper understanding of technology than the often-clueless Republicans and Democrats, and we could ensure that this remains true in the future.

But most important, the libertarians have the right ideas—about the wisdom of relying on the market, about the futility of central planning, about the practical importance of liberty for innovation and growth, in our industry as well as others—that I believe we'll have to embrace, sooner or later, if we want to realize the opportunities ahead of us in the 21st century. These ideas are important to everyone in our economy and culture, but they are critical to the computer industry. We have been held back, co-opted, and bamboozled for too long by today's very disappointing political leaders. It is time for us to get involved. . . .

What would this mean in the long run? It would mean that we could worry less about politics. It would mean we could focus on creating new technology, designing and building great products, and meeting customers' needs and wants once again.

I admit that as a political start-up, the libertarian movement may seem like a long shot compared to just coping as best we can with the Democrat-Republican duopoly. Just think of it like Apple versus Texas Instruments in 1978, or Microsoft versus IBM in 1982. In my view, the libertarians may be the only real alternative we have to becoming just another industry that is caught up in the stasis of American politics—the only way to get hope out of the bottom of Pandora's box. □

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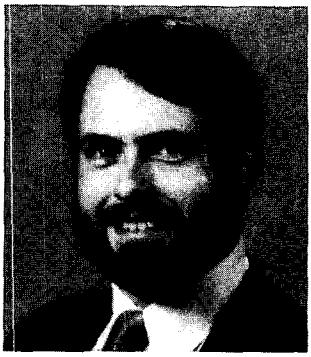

Murderous Nostalgia

Among America's more significant actors and singers was Paul Robeson, born a century ago. His centennial is being celebrated with film retrospectives, museum showings, and book reissues.

Robeson, an impressive talent who struggled against pervasive racism, had a less presentable side: he was an avowed communist. He promoted leftist causes in the United States, frequently visited the Soviet Union, and was awarded the Stalin Peace Prize in 1952.

Anyone can make a mistake, but Robeson knew what he was doing. In 1949 he met in Moscow with his friend Itzik Feffer, a Yiddish author who warned of the start of Stalin's anti-Semitic purges. When Robeson returned home, he told reporters that "I heard no word about" anti-Semitism. He later accepted the Stalin Peace Prize despite Feffer's murder at the hands of the regime.

It is impossible to know how Robeson, who died in 1976, would have reacted to the collapse of communism. But true believers remain. Sunset Hall in Los Angeles, a small apartment home for the aged begun 75 years ago by Unitarians, could provide the plot for a [illegible]

trial of Julius and Ethel Rosenberg, Soviet atomic spies in the United States who were executed early in the Cold War.

Sunset's residents demonstrate on behalf of janitors' pay, lobby for Social Security, endorse national health insurance, circulate petitions over Sunset Hall's dismissal of an employee, object to the purchase of tablecloths as wasteful, and collectively decide what food is to be served. But they don't just want more government in a liberal democracy. They pine for the good ol' days of communism—the real thing.

At age eight Glady Foreman, now 90, was proclaimed a "little socialist" by her father. She has written a book—as yet mercifully unpublished—titled "How Adam and Eve Lost Their Social Security." Says Foreman: "Socialism, crushed to the earth, will rise again."

Jacob Darnov, a messenger in the Bolshevik army decades ago, expresses his continuing admiration for Lenin. "He's the greatest politician we ever had in this world."

Wayne Friedlander, a former member of Students for a Democratic Society who once ran Sunset Hall, says he owes the residents a [illegible]

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implementation is inherently destructive and violent. Everywhere and every time, the experience has resulted in a charnel house. To support communism still, despite decades of mass murder, is inexplicable.

In his book, *Death by Government*, University of Hawaii professor R.J. Rummel catalogues the catastrophic record of the regimes so beloved by Sunset Hall residents. The Soviet Union, figures Rummel, killed somewhere between 28 million and 127 million people. His best estimate is 62 million. Even those who believe that Rummel's figures are exaggerated still offer mind-numbing figures—20 million, according to French scholar Stephane Courtois's *Black Book of Communism*.

Rummel figures that the second most murderous regime, also surpassing the Nazis, was that of Mao Zedong. Rummel estimates that the communist Chinese killed somewhere between six million and 102 million people—most likely about 35 million. Courtois actually puts Mao Zedong in first place, with between 45 million and 72 million dead. Rummel and Courtois also offer estimates for other great communist killers. Cambodia's Khmer Rouge, led by Pol Pot, wiped out an estimated two million to 2.3 million people; the Vietnamese murdered 1 million to 1.7 million, while the North Korean regime killed 1.7 million to two million.

There's more. Communist Poland slaughtered 1.6 million (through extensive ethnic cleansing after World War II). At about the same time, Yugoslavia killed around 1.1 million. African governments have accounted for 1.7 million.

Then there were the many lesser communist tyrannies that dotted Asia and Eastern Europe. In some of those states the dead numbered "only" in the hundreds of thousands. In a few, "merely" tens of thousands—truly representing the velvet glove of communism. But Glady Foreman still hopes that socialism "will rise again."

It is astounding enough that true believers remain. What could prompt the *New York Times* to put a story about Sunset Hall on its front page, however? Observes syndicated columnist Michael Kelly, "If a *Times* reporter found a brave little band of aging Nazis, who kept a bust of Hitler in the living room and who declared that fascism would rise again, and wrote this up cute—well, this simply could never happen." He's right, even though there is no difference in the moral culpability of the true believers of left and right.

Indeed, the ongoing effort to rehabilitate former communists suffers the same myopia. There are, for instance, the Rosenbergs. A number of leftists long proclaimed the Rosenbergs' innocence. Unfortunately for the true believers, Soviet archives indicate that the husband-and-wife team were, yes, spies. The long campaign conducted on behalf of Alger Hiss, a Soviet spy convicted of perjury after serving in the State Department, also ground to an ignominious close with overwhelming evidence of his guilt.

Then there are those who were blacklisted by Hollywood during the Cold War. Many did suffer, and suffer unfairly. But private sanction is very different from public prosecution. The national security state committed excesses; the refusal of some studios to hire apparent communists was something quite different. Indeed, those who laud the blacklisted writers often act as if being denied public credit for one's script, a common result of blacklisting, was akin to being sent to the Gulag—as were tens of millions by the rulers so beloved by those who were blacklisted.

This is the central issue. As the *Washington Post*'s Stephen Rosenfeld points out, "What is missing from the discussion is an evaluation of the substance of the political views many of the movie people had." Those blacklisted were supporting a monstrous tyranny, one that oppressed, slaughtered, and destroyed at will. That someone would refuse to hire them is as unsurprising as, say, refusing to hire a professing Nazi. The real victims were the tens of millions gunned down by tyrants.

The twentieth century, filled with so much horror, is mercifully coming to an end. While we may choose to forgive those who supported the murderous totalitarians who wreaked human devastation, we should never forget. However charming, talented, or even cute they now may seem to be, their hands remain covered with blood. □

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THE FREEMAN
Ideas On Liberty

The Mother of All Food Fights

by Sam Kazman

Someone once commented that if the federal government regulated restaurant fare, there'd be blood in the streets. Vegetarians would be fighting with meat-eaters, Jews and Moslems would battle pork fanciers, teetotalers would have at it with imbibers, and burrito purists would persecute wrap-sandwich snackers. Food peace is, in fact, one of the greatly unappreciated benefits of our relatively free restaurant market. Violent food fights are few and far between, and they tend to be limited to such government monopoly situations as prisons.

The U.S. Department of Agriculture, however, recently came close to igniting the mother of all food fights with its organic-food labeling proceeding. The rulemaking drew over 115,000 comments—a record for the agency. At issue were such questions as whether the term *organic* could be applied to such items as genetically modified foods, irradiated meat, or crops fertilized with municipal sludge. Even the eligibility of livestock raised under confined conditions was questioned.

One might wonder why USDA was involved in this issue in the first place. A government attempt to define organic food nowadays is little different from a government attempt to regulate religious doctrine; it might bring uniformity, but it might also ignite the supermarket equivalent of a religious war. USDA, however, had not plucked this issue out of thin air. Rather, the task had been handed to it by Congress in the 1990 Organic Foods Production Act. The agency might have told Congress, "forget it," but agencies are loath to be that candid about nonsensical missions. On the contrary, a little extra turf and budget never hurt anyone in government service.

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The Elusive Meaning of Organic

So what is *organic* anyway? The simplest definition is the one we learned in high school—compounds that contain carbon. That definition is also the most useless, since it encompasses just about everything we consume other than water and salt. (Is sea salt ever marketed as organic?)

The popular notion is that organic food contains no synthetic chemical additives. Defining just what this means in practice is hard enough. Are there any permissible measurable residues? How far down the production chain do the rules apply? If a field had synthetic pesticides applied to it in the past, how much time must pass before the produce grown on it can be called organic? What about the trace amounts of preservatives present in plastic packaging?

Moreover, even this basic public understanding—that organic means no synthetic additives—is subject to exceptions by organic purists. USDA's main organic-advisory board, for example, issued a lengthy series of recom-

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mendations regarding permissible synthetic substances and impermissible nonsynthetic substances.

But what the controversy over USDA's proposal demonstrates is not that organic food may be technically difficult to define, but that it isn't a technical concept at all; instead, it has become a theological one. For many people, organic has come to mean a way of life—in the words of one group, a "holistic approach" involving "key concepts such as health of the agro-system and biodiversity."

The fact that these concepts may be hard to define does not mean that the people who espouse them are insincere; it simply highlights the folly of federal involvement.

Private Certifiers

As demand for organic food has grown, private organic-certifying agencies have arisen. Some have stricter standards than others, and some may have standards and enforcement practices so lenient that they are practically meaningless. But to the extent that differences between them really mean something to consumers, those consumers are fully capable of distinguishing between them (or of choosing retailers who do the job for them). Regardless of whether we view the popularity of organic food as a crazy fad, a long-term market development, or an evolving esthetic, two things are clear: producers and consumers are entitled to pursue it, and government should keep out.

The lack of any pressing necessity for such involvement is clear. The large organic-foodstore chains already have established connections with suppliers and certifying agencies; the same is true of conventional supermarket chains that carry organic products. In the words of one marketing director, "consumers won't see any drastic changes in our stores" under a federal rule. "We've been taking a very strong stance on organic from the beginning, requiring certification from growers."

Organic growers themselves are also capable of doing without a cumbersome federal definition. According to one organic-farming newsletter, "many growers say that if certified organic becomes too difficult, or meaningless, they will just use another word to market their produce."

The issue has been complicated by the entry of several state agencies into the certification business. The basic political urge of such agencies is to pre-empt the field and create regional monopolies over the term *organic*. To the extent this urge is resisted, consumers are better off.

Consumers who care about such issues don't need the force of law in order to obtain the information they want about food products. USDA has already announced that its eventual definition will not allow genetically modified foods, but suppose it had ruled otherwise. Producers of organic foods that were *not* genetically modified could still communicate that fact to interested consumers—through labeling, through advertising, and even through private organic-certification systems that make a point of prohibiting bioengineered products. Information that groups of consumers want will make its way to them without legal compulsion.

In a sense, this is exactly what has happened for kosher certification. When it comes to kosher food, some people couldn't care less, some people care only that a product be labeled kosher, and some are concerned about the strictness of the standard met by the product. For this last group there are competing rabbinical inspection boards, each with a different logo. With the possible exception of guarding against outright fraud, there is little need for government involvement. Interestingly enough, despite the lack of that involvement, consumer demand for kosher certification is so high that it has "gone mainstream." Kosher-product sales have been growing steadily (in dollar volume they are only slightly behind organic food), and such mass marketers as Nabisco and Mars have recently joined the trend. Consumers seem capable of sorting things out peacefully.

Which brings me back to my opening point about restaurant regulation and public peace. I read it somewhere, but I don't recall where. For the first reader to identify the source, I will buy a sandwich: veggie, organic, kosher, cheese and onions, you name it. □

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THE FREEMAN
Ideas On Liberty

The IRS, Now and Forever?

by James Bovard

Since late last year, politicians in Washington, D.C., have been promising to save Americans from the Internal Revenue Service—to fundamentally reform the agency, once and for all. The surge of anti-IRS outrage fits a dismal pattern in recent American history. On July 30, 1996, when signing a bill to provide meager additional protections to taxpayers, President Bill Clinton proclaimed: "We say to America's taxpayers, when you deal with the IRS, you also have privileges and we respect them. You have protection and we will help provide it. You have rights and we will shield them."

We've heard this before. Since the 1960s, national outrage has repeatedly erupted when news of IRS abuses hit newspaper front pages. Each time, politicians and bureaucrats swore that they would fix the problems and that such abuses would never happen again. Each time, the IRS has continued to tyrannize and terrorize innocent American citizens—with no effective redress from either federal judges or from the U.S. Congress.

We will examine some of the more brazen IRS abuses to gain insights into the futility of moderate reform.

Institutional Arbitrariness

Roughly two million Americans are audited each year. While many Americans might presume that the tax-audit process is an even-handed pursuit of a fair tax assessment, many IRS agents see it as a chance to get a pound of flesh from an innocent taxpayer. IRS auditors are rewarded on the basis of how much additional tax they impose on people, not on whether they follow federal tax law. The IRS's "Program Letter for Fiscal Year 1997" stated that tax examiners will be evaluated according to the total "proposed additional tax and penalties" they recommend for imposition on taxpayers, as well as "total revenue protected: Total dollars protected as a result of disallowing claims for refund." The American Institute of Certified Public Accountants (AICPA) complained in 1997 to the IRS that "The Service's methods of evaluating its personnel focus on . . . maximizing revenue and protecting the Treasury." AICPA added that "the Examination Division's performance is evaluated solely based upon factors other than determinations as to the proper amount of tax."

When individuals appeal audit findings to the IRS Appeals Office, it sustains barely 30 cents on the dollar of additional taxes assessed during audits. In other words, almost 70 cents of each dollar of additional taxes that auditors demand is found to be unjustified. In percentage terms, the IRS apparently cheats far more often during tax audits than average Americans cheat on their tax returns. The National Commission on Restructuring the IRS found that the quality of IRS audit work has deteriorated in recent

James Bovard is the author of Lost Rights: The Destruction of American Liberty *(St. Martin's, 1994) and* Shakedown *(Viking, 1995).*

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November 1998

The Danger of Deifying the State

Until this afternoon, I had planned to write this month about the folly of Social Security, or about the perils of central banking, or about the internal contradictions of government regulation; I forget which, exactly. I forget because a far more interesting topic sprang to mind a few hours ago: my son, 15-month-old Thomas Macaulay Boudreaux.

This afternoon I watched Thomas toddle joyfully about the playground in our hometown of Irvington-on-Hudson. He pointed quizzically at the geese squawking near the water's edge; he was entranced by an acorn; he laughed and laughed as we slid down a sliding board; and he studied with the seriousness of a surgeon the sand that he held for the first time in his tiny hands. I was overcome with the joy that parents feel when they see their children learning how wonderful life can be. And intense affection washed over me as I saw him make his way across the grass while prattling his sweet non-words.

Just as Thomas paused and looked back to ensure that I was still there—just as his eyes met mine—my mood completely changed. For reasons I do not know, at that moment my mind recalled what is for me the most vivid and horrible scene in Steven Spielberg's film *Schindler's List*. The scene shows Nazi trucks stuffed with frightened children being forcibly taken from their parents—parents left standing in a detention yard, screaming and wailing, as they helplessly watch as their little ones are driven off to no-one-knows-where.

Recollecting that single movie scene and knowing that it depicts a reality less than 60 years past caused me to shake physically. The pain even of *imagining* such a horror was acute.

I ran to Thomas and held him tightly. He slobbered on my cheek as I laughed and cried simultaneously. "My boy is here, safe, with me," I repeated to myself.

"But what if they come?" asked the darker part of my mind. "What if one day such beasts show up in America to take Thomas from me as if he were trash on the curb?"

The calmer part of my mind assured me that no such beasts are darkening the horizon.

As I strolled Thomas back home, however, I wondered. I wondered about the source of such brutal totalitarianism. If such vileness arose during this century in Germany (and in Russia, and in China, and in Cuba, and in other countries too numerous to list), are we Americans really

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secure against the scourge of unlimited totalitarianism?

It's unthinkable that in 1998 the U.S. government will engage in Nazi-style beastliness. But it's not at all unthinkable that such brutal displays will become commonplace in America sometime in the future. Totalitarianism is inevitable if enough people come to believe that government's proper role is to solve all problems. A people who demand that their government engineer them into a state of collective holiness will in fact end up in an earthly hell.

Consider the powers that are today exercised in America by the national government. In the name of water conservation, Washington specifies the amount of water that our toilet tanks can hold. In the name of ecology, Washington micromanages private use of privately owned lands. In the name of fairness to the handicapped, Washington intrudes itself into the building-design business. In the name of child safety, Washington vetoes parents' choices of which toys to buy for their children. In the name of adult safety, Washington dictates which pharmaceuticals we may and may not use. In the name of energy conservation, Washington specifies the fuel efficiency of our automobiles. And as I write these words, Congress is considering federal legislation to override state statutes that permit people to carry concealed handguns. Fewer and fewer aspects of our lives are off-limits to Washington.

Why do we tolerate such intrusiveness from strangers—intrusiveness that none of us tolerate even from members of our own family? The reason is that Americans generally believe not only that government means well, but also that it possesses unique powers to right all wrongs. In short, too many Americans believe government to be godlike.

Thus the danger: that which we deify we trust without question. But government is an institution of mortals, not of gods or quasi-gods. When anyone treats another person as being more-than-mortal, he who is ludicrously elevated in this way suffers an inflated ego. And he who treats others as more-than-mortal suffers a correspondingly deflated sense of self-respect and loses his independence of mind. The initial sentiment of those who are elevated might be a warm paternalism toward those who do the elevation. But if not removed from their perch, the elevated inevitably come to regard all others as clay to be beaten, molded, and baked into whatever shapes the elevated happen to fancy.

Modern totalitarianism grows from the dangerously wrongheaded belief that those who wield government power are somehow greater than, wiser than, and more trustworthy than ordinary men and women. And it is fertilized by the childish wish that every inconvenience no matter how minor, every affront no matter how innocent, and every possible danger (except that of the state itself!) no matter how remote be prevented by government.

People who are ceded the power necessary to engineer society eventually become monsters.

This eventuality is what I fear as I look at my little son. He is safe today. But if I reflect upon all the power that government wields now that it did not wield when I was born 40 years ago, and then consider the real possibility that government's power will grow at the same pace over the next 40 years, I tremble with fright. A government with such power would assuredly treat Thomas and his children, not as humans, but as cattle or clay. And if Thomas should resist by asserting his individuality, the government would summarily slaughter him along with all the rest of those truly heroic people who refuse to be babied or bullied by the state.

No calling for me is higher than warning against the awful dangers of statism. Nothing less than my son's life depends upon reversing the modern trend of deifying government.

Donald J. Boudreaux
President

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FEE Holiday Sale: Readers' Favorites

Once again the holiday season is upon us. This month we're offering for sale titles that you, our readers, love (next month look for staff favorites). We hope that you'll consider purchasing one, two, or twelve of these great works and give them as gifts to a) other freedom lovers; b) statists who need to hear the other side; c) family members or friends; or, d) your local library. Over the years these books have proved themselves to be highly readable, enjoyable expositions of economic wisdom and individual liberty. Go ahead, stuff some stockings with a different kind of sweet!

Human Action, 4th ed. — What better place to begin than with Ludwig von Mises! While *Human Action* definitely WILL NOT fit into your — or anyone else's — stocking, we nonetheless feel that this great work is worthy of your consideration as a holiday gift. The beautiful navy blue leather-bound edition will make an ideal present for a child, grandchild, or beloved other who is interested in the hows and whys of market processes. As we noted last month, Rose Wilder Lane praised this book as "unquestionably the most powerful product of the human mind in our time" and believed it would "change human life for the better during the coming centuries as profoundly as Marxism has changed our lives for the worse in this century." Why not give this exceptional work to someone exceptional in your life?

Deluxe leather ~~$99.95~~ **Sale: $49.95 — save 50%!**

Economics in One Lesson - 50th Anniversary Edition — Henry Hazlitt's work is undeniably a classic. Building on Frederic Bastiat's distinction between "the seen and the unseen," Hazlitt teaches readers the key "lesson" of economics — that you **must** look beyond the immediate, obvious results of actions to understand their full impact. (If only economics reporters on TV would learn this lesson we would no longer be insulted by reports of the "silver lining" around the cloud of natural disasters — that carpenters, at least, will have more work!) This great book explains, among other things, how the price system works, the effects of minimum wages, who is protected by "protectionist" tariffs, and how taxes discourage production. Follow the lead of some George Mason University professors who use this book to teach undergraduates economics!

205 pages, cloth ~~$14.95~~ **Sale $9.00**
paper ~~$9.95~~ **Sale $5.00**

Clichés of Politics — Edited by Mark Spangler, *Clichés* is now in its fourth printing, and for good reason. This excellent book refutes classic "clichés" we've all heard statists use to explain why we need more government and, therefore, more coercion. Here's a very brief sampling: "The size of the national debt doesn't matter because we owe it to ourselves"; "There is too much inequality of wealth and income"; "If free enterprise really works, why the Great Depression?" and most persistent and pernicious "To solve the problem we need government regulation." George Roche, president of Hillsdale College, calls *Clichés* "**the** best brief anthology of economic principles available today." Get several copies, pass them around, and watch the intellectual sparks fly.

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The Mainspring of Human Progress (50th Anniversary Edition) — Another of our consistent best sellers, Henry Grady Weaver's little gem of a book (this one **could** fit in the stockings) goes beyond economics in explaining the human progress made possible by the commericial and industrial revolutions. Weaver explores the truly important question of why countless human beings starved to death for thousands of years, but now, at least in the developed world, we no longer do. Identifying individual liberty and private-property rights as keys to economic growth and human well-being, Weaver provides an eloquent defense of the free-market system.

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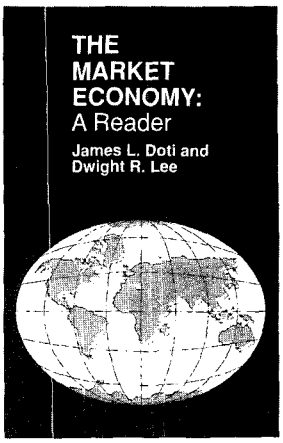
The Market Economy: A Reader

edited by James L. Doti & Dwight R. Lee



Looking for a great way to teach economics, or learn it yourself?

This outstanding anthology is an invaluable source book for students of free-market economics as well as for proponents of limited government.

Professors Doti and Lee have assembled a stellar list of authors—Adam Smith, Frederic Bastiat, David Ricardo (among the classical economists); Ronald Coase, Milton Friedman, James Buchanan, F.A. Hayek, Ludwig von Mises, and George Stigler (among the modern greats); in addition to Ayn Rand, Henry David Thoreau, and Charles Murray, among others—to explain eight key issues: the invisible hand; markets and individual freedom; government regulation; the proper role of government; international trade; scarcity and social cooperation; income distribution; and imperfect markets.

What a joy to find—in a single book—Hayek's classic essay "The Use of Knowledge in Society," Friedman and Stigler's wonderful work on rent control "Roofs or Ceilings?", Ayn Rand's essay on "The Nature of Government," and Adam Smith's pivotal analysis of the division of labor.

For anyone homeschooling children, or for anyone interested in deepening his or her knowledge of the relationship between economics and personal freedom, this book is not only essential, it's a real treasure.

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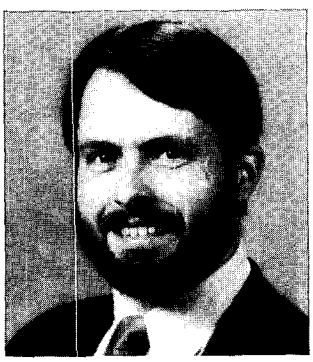
An Evening at FEE with Doug Bandow

THE POLITICS OF ENVY



Saturday, November 14, 1998

What's really going on in Washington today? What does the current mess tell us about politics in general? *Freeman* columnist Doug Bandow diagnoses the malady—and prescribes a cure: limited government.

Don't miss this lively roundtable at The Foundation for Economic Education, 30 South Broadway, Irvington-on-Hudson, New York. This informal get-together starts at 5 p.m. with a reception and dinner, followed by Doug's presentation and a question-and-answer session. Price is $35 per person.

For reservations, call Janette Brown at (800) 452-3518.

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years in part because of poor training of auditors and the increasing complexity of the tax law.

The incentive system is truly bizarre: IRS auditors receive bonuses for assessing additional taxes regardless of whether appeals officers determine that citizens actually owe such taxes. Dan Pilla, author of several books on the IRS, estimates that Americans pay billions of dollars in taxes that they do not owe because few taxpayers take their audit case to the appeals level. Expense and fear deter many appeals.

IRS Culture

Why are abuses of taxpayers so common? In recent years, IRS agents have been indoctrinated to see taxpayers as a class enemy. This new attitude is epitomized by "Culture Bingo"—a game used to train agents and auditors to recognize "an IRS organizational culture regarding the audit process." The game encourages the use of summonses to obtain third-party records, to think of fraud referrals as a path to promotion, and to believe that most taxpayers deposit unreported receipts in their bank accounts. One of the most damning lessons of the training is the doctrine: "Taxpayers seem to live better than I do." The IRS appears to be officially seeking to maximize the resentment or hostility that agents feel toward the taxpayers they audit. The American Institute of Certified Public Accountants said of the course materials: "Every ethical issue presented finds the ethical result to be pro-IRS and anti-taxpayer. There is not one scenario where an IRS agent might act unethically against a taxpayer's interest."

In 1988, Congress prohibited the IRS from evaluating its employees on the basis of the additional taxes they collected. However, the IRS has—as usual—flouted this law and used statistical evaluations that help turn IRS agents into public enemies. One confidential IRS document uncovered last fall revealed that auditors in the San Francisco region were expected to assess at least $1,012 in additional taxes for each hour they spent auditing a taxpayer's return. Any auditor who failed to achieve that goal could lose cash bonuses or promotions. Joseph Lane of the National Association of Enrolled Agents (licensed taxpayer representatives) declared: "Whenever an enforcement agency resorts to using production statistics for evaluative purposes, be they audit yields or traffic tickets, the first casualty is citizen rights."

There are practically no limits to the scams that the IRS can use to jack up the amount of tax citizens supposedly owe. If a taxpayer falsely reports his income, he can be sent to prison for several years for tax fraud. But if an IRS employee lies about federal tax law in order to commandeer more of a citizen's bank account, he can get a bonus award and maybe even a promotion. IRS auditors disallow legitimate expenses—such as in the case of a California restaurant owner who was prohibited from counting food purchased for his restaurant as a business expense. In auditing the returns of self-employed salespeople, IRS agents have refused to permit as business costs the expenses for trips in which a sale did not occur.

Increasingly, IRS auditors are simply making up income—and then demanding that people pay the additional taxes. IRS agents use Bureau of Labor Statistics data to determine the average income in a certain geographical area. If they are not satisfied with the additional taxes they have been able to gin up for someone they are auditing, they announce that the person is hiding income—that the person actually has the average income in his area—and thus owes thousands of dollars of additional taxes, penalties, and interest. As Bruce Strauss, a private tax preparer who worked for IRS collections for over 30 years, recently observed: the fact that "the IRS now has the authority to assign additional income to a taxpayer at its discretion, without any basis in fact, is frightening and absolutely unacceptable."

Property Seizures

IRS officials insisted at Senate Finance hearings last year that employees were not encouraged to seize private property merely to accumulate bonus points on the job—a

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practice strictly prohibited by federal law. However, subsequent audits of the IRS have shredded that defense. An audit released in December of the IRS's Oklahoma-Arkansas district found that a third of the property seizures violated federal law or IRS regulations. The report concluded: "District management's goals and performance expectations are focused heavily on specific statistical targets, including dollar targets" per employee. IRS revenue officers ignored regulations and guidelines before seizing property; in one case, the only effort an IRS agent made to contact a citizen before confiscating two cars "consisted of driving to the taxpayer's house, honking his car horn, and noting that no one came out of the house in response."

In recent years, the IRS has greatly increased its audit rate for low-income families, at the same time that the audit rate for wealthy Americans has fallen. One IRS criminal investigator told the Senate last September that the Criminal Investigation Division management "encourages and emphasizes . . . what they referred to as mom and pop cases, which are easy hits and can be opened and closed quickly . . . rather than investing time in the large cases which require more time and resources to prove."

The IRS has had a special preference for pursuing divorced people. After a divorce, the agency has hounded both former spouses to force each of them to pay the full amount they allegedly owed as a couple. The General Accounting Office estimated that the IRS wrongfully pursues tens of thousands ex-spouses each year, demanding additional tax payments that are not legitimately owed. Senator Bill Roth observed that "the agency is all too often electing to go after those who would be considered innocent spouses because they are easier to locate, as well as less inclined and able to fight."

Sometimes, the first time a person knows the IRS is on his case is when he gets a call from the bank saying that his savings have been commandeered by the agency. The IRS is not required to tell people when it confiscates their bank accounts; it claims that the only "official notice" people are entitled to is a notice from the bank.

The Mirage of Taxpayer Rights

Time and again, the American people have been deceived by political promises to fix the IRS. In 1988, and again in 1996, Congress enacted so-called Taxpayer Bill of Rights legislation that was supposed to stop the IRS from tyrannizing innocent citizens. However, according to training materials the IRS uses for new agents, the main effect of the bills of rights is to *increase* the agency's power over taxpayers. The American Institute for Certified Public Accountants recently complained, "In turning the Taxpayer Bill of Rights on its head, [IRS] examiners come away believing that, with no legal opposition, they will be free to . . . interrogate taxpayers and invade taxpayers' rights of privacy by interviewing 'spouses, relatives, employees, friends, competitors' and a host of others."

An IRS collections officer with a quarter-century experience testified anonymously at the Senate hearing that the Taxpayer Bill of Rights has "had very little effect on the conduct of the IRS. The Taxpayer Bill of Rights is very positive . . . but who is going to enforce this for the taxpayer? If you're going to sue the IRS it'll take thirty, forty, fifty thousand dollars." Phoenix tax lawyer Bob Kamman observed: "The taxpayer rights provisions of the Internal Revenue Code are like the civil rights provisions of the former Soviet Union's constitution. On paper, they tell a wonderful story. In practice, for many taxpayers there is no effective protection against government abuse."

For instance, the 1988 Taxpayer Bill of Rights created a Taxpayer Ombudsman with the power to issue a "taxpayer assistance order" to provide immediate relief in cases where taxpayers were being wronged by the IRS. However, as usual in Washington, this appointee has become a lapdog of the agency he is supposed to oversee. In 1996, over 32,000 taxpayers requested "taxpayer assistance orders"; the Ombudsman granted them in only five cases—slightly more than one in every 10,000 requests.

The only Americans who have legal rights, in the IRS's eyes, are those who can afford to hire lawyers and topnotch accountants to fight

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the agency. Congress enacted provisions to allow citizens who fight the IRS in court to have their attorneys' fees paid in cases where the IRS's position lacked merit. However, the IRS and the Justice Department have fought tooth and nail to prevent almost anyone from receiving reimbursement for their legal fees in any case—regardless of how egregious the government's behavior may have been, and regardless of how often the IRS may have previously lost in court on exactly the same issue. The fact that the cost of hiring a lawyer and fighting the IRS in court is prohibitively high for the vast majority of Americans means that the IRS has carte blanche to ride roughshod over most Americans' legal rights.

The Latest Bill of Rights

Last summer, Congress passed and President Clinton signed an IRS overhaul bill that supposedly gives taxpayers all the protection they need from federal revenue collectors. The fact that this third "bill of rights" in ten years passed Congress by overwhelming margins (402-8 in the House, 96-2 in the Senate) indicates that it is unlikely to reduce the federal government's fundamental power over private citizens. The new law does shift the burden of proof for some tax-court cases—but only a tiny percentage of taxpayers who are wrongfully assessed for additional taxes fight all the way through IRS administrative procedures to a courtroom. The law provides some relief to divorced people whose deadbeat ex-spouses have left them tax troubles, and extends attorney-client privileges to certified public accountants. The law also creates a new oversight board—but the National Treasury Employees Union, which represents IRS workers, is guaranteed a seat on the board. Moreover, the board will only be concerned with long-term planning and budgets, not today's abuses.

Senator Daniel Patrick Moynihan said that the purpose of the law was to give IRS agents "the respect to which they are entitled." Yet, the IRS's own audit reports and congressional hearings preceding the bill's passage raised one horror story after another of IRS agents on rampages. After the Senate passed the bill, IRS Commissioner Charles O. Rossotti and Treasury Secretary Robert Rubin praised the bill. Yet Rubin had vigorously attempted to derail the first Senate hearings on IRS abuses in September 1997, and Rossotti had downplayed the extent of IRS abuses in his own testimony at later hearings. With powerful IRS friends like Rubin and Rossotti, taxpayers have no reason to presume their problems have been solved.

Congressional and administrative "fixes" of IRS abuses are a pipe dream because the agency will continue to have vast arbitrary power over ordinary Americans. Nancy Jacobs, who along with her husband was hounded by the IRS for 16 years because the IRS provided an incorrect identification number to her husband's optometry business, declared: "When you have someone come to you from the IRS telling you they're going to take your home, take your vehicles—everything you own, close your business—you do what they say." The IRS has indisputably and grossly abused every bit of power that Congress has given it. A grant of power from Congress to the IRS is just the starting point; it then stretches the power to the limit. When it is accused of savaging the lives of taxpayers, it proclaims "good faith" error.

It is an illusion that better laws will solve the problems of an agency that is long notorious for breaking any and all laws. The only truly effective reform is to shut down the IRS and get rid of the byzantine tax code designed to allow politicians and bureaucrats to micro-manage the lives of American citizens. □

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THE FREEMAN
Ideas On Liberty

Another Minimum-Wage Clash

by Richard B. McKenzie

It happened again. Republicans and Democrats recently locked political horns over President Clinton's proposed one-dollar increase in the minimum wage. The political partisans repeated past claims with self-righteous fervor, but once again were off base on the consequences of the increase. (The measure was defeated—this time.)

President Clinton and his Democratic allies argued that the proposal would be an unmitigated blessing for the country's low-wage workers who deserve an increase in their take-home income. Bob Herbert, a columnist for the *New York Times* and an avid minimum-wage supporter, quoted approvingly a study from the Economic Policy Institute (EPI) which found that the last hike raised the incomes of 10 million Americans: "The benefits of the increase disproportionately help those working households at the bottom of the income scale. Although households in the bottom 20 percent (whose average income was $15,728 in 1996) received only 5 percent of total national income, 35 percent of the benefits from the minimum wage increase went to these workers."

Herbert is convinced that such findings should give minimum-wage critics reason to eat their words. He reminds his readers of what Cato Institute chairman William Niskanen said during the last debate over the minimum wage: "It is hard to explain the continued support for increasing the minimum wage by those interested in helping the working poor."

Despite EPI's claims, the Republicans argued, as they have in the past, that if Congress raised the cost of menial labor, several hundred thousand jobs would be lost. Some employers would not be able to afford as many workers, and other employers could be expected to automate low-skill jobs out of existence. Opponents backed up their claims with equally sophisticated statistical studies that showed that some low-skilled workers should be made better off (those who kept their jobs) but only because other low-skilled workers would be made worse off (those who are unemployed). For example, the EPI commissioned a study of a $1.35 increase in the minimum wage in the state of Washington and found that by 2000, the increase can be expected to destroy 7,431 jobs, causing the affected workers to lose $64 million in annual income.

Both Sides Are Wrong

Both sides to the debate were once again wrong in their assessments of the minimum-wage increase because they both failed to recognize that employers are a lot smarter than the political combatants seem to think. Neither side seems to realize that Washington simply doesn't have the requisite power over markets to significantly improve worker welfare by wage decrees, no matter how well-intentioned the legislation may be.

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Why is this so? The simple answer is that the labor markets for low-skilled workers are highly competitive, which explains the low wages paid menial workers in the first place. Many employers of low-skilled workers would love to be able to pay their workers more, but they have to face a market reality: if they paid more, then their competitors would have a cost advantage.

When Congress forces employers to pay more in money wages, it also forces them to pay less in other forms, most notably in fringe benefits. If there are few fringes to take away, employers can always increase work demands.

Why would employers curb benefits and increase demands? First, they *can* do it, given that the minimum-wage hike initially will attract more workers and cause some employers to question whether they can hire as many workers unless adjustments are made. The forced wage hike also strengthens the bargaining position of employers, given that they can tell prospective workers, "If you don't like it, I can hire someone else." Second, the employers *must* cut fringes and/or increase work demands, or face the threat of losing their market positions to competitors who do so. Third, if employers don't cut fringes and/or increase work demands, the value of the company's stock will suffer, creating profitable opportunities for investors to buy the firm, change the benefit/work-demand policies, improve profitability, and then sell the firm at a higher price.

The net effect of the adjustments in fringes and work demands is that the cost impact of the minimum-wage hike to the employer will be largely neutralized. For example, when the minimum wage is raised by a dollar, the cost of labor, on balance, may rise by only five cents. That explains why studies have found that recent minimum-wage hikes have caused few (if any) job losses even among that group of workers—teenagers working at fast-food restaurants—whose jobs are most likely to be cut. Even the EPI study cited above shows a reduction in Washington state's total employment of less than three-tenths of one percent for a proposed 26 percent increase in the state's minimum wage.

This line of argument can also help us understand why workers who retain their jobs are unlikely to be any better off. They get more money, but they get fewer fringes and have to work harder for their pay. The only reason a sane employer would offer the fringes and reduced work in the first place is that the workers valued them more highly than they valued the money wages that they gave up to get them. And sane employers aren't about to offer workers anything unless they get something in return, like greater production or a lower wage bill. When the minimum wage is hiked, therefore, the value of the resulting lost fringes and reduced work demands to the workers will be greater than the value of the additional money income.

Put another way, the workers who retain their jobs are made worse off (albeit marginally so) in spite of the money-wage increase. Employment in menial jobs may go down (albeit ever so slightly) in the face of minimum-wage increases not so much because the employers don't want to offer the jobs (as traditionally argued), but because fewer workers want the menial jobs that are offered. Understandably, the voluntary quit rate among low-wage workers goes up, not down, when the minimum wage is hiked.

Seen from this perspective, the Economic Policy Institute figures on the added income received by 10 million workers are grossly misleading because they suggest that the affected workers are better off, which is unlikely.

Granted, economists might speculate that the job reductions have been small because the demand for menial labor is fairly constant, but that explanation makes no sense. The elasticity of demand for anything, including labor, relates to the number of substitutes: the more substitutes, the greater the elasticity. The problem with the explanation is that there is no labor group that has more substitutes than menial (minimum-wage) workers, especially now that firms have so much flexibility to automate jobs out of existence or to replace domestic workers with foreign workers by way of imports.

You can't fool the market. It will outsmart the smartest of politicians. □

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Current Issues

Service Without a Smile

Stop the presses! Here's a news flash that will send shock waves through the country: school-based compulsory community service doesn't engender the spirit of giving. Imagine that! When students are forced to be compassionate volunteers, they rebel and find ways to get around the system. Who'd have believed it?

In a recent article in the *Washington Post*, James Youniss and Miranda Yates are crestfallen because "a good idea is in danger of being subverted." For six years the Maryland Board of Education has required students to perform 75 hours of community service before they can graduate from its schools. (Other districts around the country have similar programs.) But according to Youniss and Yates, "many are evading the requirement by meeting the letter, but not the spirit, of the law." And some "students treat service as just another credential for their college applications." Hard to believe, but there it is.

How are they evading their mandatory good deeds? The authors say students look for ways to "get the task over with as quickly and painlessly as possible." Others want credit for activities such as babysitting, taking out the family's trash, mowing a neighbor's lawn, or setting up a dance at their schools. Youniss and Yates report that last year students who had put off doing their service were permitted at the last minute to satisfy the requirement by picking up litter on school grounds or reshelving books at the library. The authors write that "One 18-year-old student added that he would dig ditches but did not want to do anything involving people."

This is not what the architects of "mandatory volunteerism" had in mind. They seem genuinely surprised at the results. If we are to believe them, they actually expected students, on command, to be overcome with charity and good will.

People who feel a general benevolence might wish to volunteer and help out others who are in some kind of difficulty. But it doesn't follow that if people are forced by a bureaucracy to render service, they will become benevolent. They are more likely to be resentful of the imposition and find ways to discharge their obligations in the least onerous way possible. Should we really be surprised that some students see service as merely a task they have to get through in order to graduate?

Social engineers never get the point. They persist in thinking they may enact schemes without taking into account that, just like them, others have their own preferences and aspirations. People, particularly young people, don't like to be forced. As Adam Smith wrote long ago, individuals are not pieces on a chessboard. If compelled to carry out someone else's plan, they will resist or evade. Let's hope that is always the case.

Youniss and Yates offer the standard defense of mandatory service: "Effective service programs give students the chance to do meaningful work that produces tangible results, such as feeding the hungry or the

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homeless, or bringing comfort to the elderly." But that's not the issue. Those opportunities exist without the school requirement. They are there for the taking. The programs don't "give" students the chance to help others. They compel students to do so. That distinction may be lost on school administrators, but it is important nonetheless.

The purpose of the mandatory service program was summarized by Nancy S. Grasmick, who was the Maryland school superintendent of education when the program began. She said that "To make a contribution to the community and learning from that contribution helps one to become a lifelong learner."

This has a phony ring to it. Whatever effects it might have, it is not clear why performing community service would instill a love of learning in children. And weren't the schools theoretically doing that already? Is there a confession here that public school isn't enough to develop an appreciation for the acquisition of knowledge?

Advocates of required service also like to tout its character-forming effects. But what about the effect of state compulsion on the character development of students? Let's not forget this is a program at compulsory government schools. First the children are forced to attend government schools, some of which are little more than custodial centers. Then they are ordered to work without pay, in the name of charity, if they want to graduate. That sounds like standard government procedure: through force all good things can be achieved.

No one seems much interested in how institutional coercion misshapes character. One would hope that the purpose of education is to teach children to become independent, responsible, rights-respecting human beings who are fit to pursue their own happiness. But the lesson taught in public schools (and, sorry to say, many private schools) is that pervasive government knows best, not only as to what and how any given child should learn, but even how a child should relate to his community.

It's hard to avoid the conclusion that mandatory service has the dual intention of marshaling manpower for approved missions and of indoctrinating students into the view that unpaid service to others is their duty. I wonder, for example, if a student would get credit for volunteering with an organization that defended property rights against statist environmentalism or that opposed the war on drugs.

We can be sure that students aren't allowed to start small businesses to fulfill their requirement Why not? Because a business exists to make money, and school-based service programs forbid compensation of any kind. (One student was told his time in the Boy Scouts didn't satisfy the requirement because he received compensation—merit badges.)

Running a small business (as a freely chosen activity) would teach some valuable lessons and would therefore be a worthwhile part of a private-school or homeschool curriculum. Students would learn that under capitalism one prospers by providing one's fellow human beings with things they need and want. Think of the corollaries that students would come to appreciate: the marketplace rests on a harmony of interests among all people; the division of labor is a method of cooperating with total strangers scattered far and wide; one man's gain is another man's gain; consent is the only proper basis for dealing with others; peace and cooperation through the market make us all richer; benevolence flows out of freedom.

Any decent school should teach those lessons. But government schools can't teach them without undermining their very reason for existence. How do you square compulsory attendance and school taxes with freedom and free markets? Government schools were set up because freedom wasn't trusted. By design they have shifted a major part of child rearing from parent to state, and have equated subservience to authority with good citizenship. The English classical liberal Richard Cobden argued in the nineteenth century that the coercive hand of an overreaching government distorts the institutions of civil society, such as trade and religion. We can surely add charity to that list. □

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THE FREEMAN
Ideas On Liberty

Do Corporations Have Social Responsibilities?

by John Hood

Businesses are accustomed to being criticized for neglecting their responsibilities to society. Complaints that private enterprise puts profit before people have long provided reliable applause lines for politicians and assorted activists, and material for the briefs of crusading public-interest attorneys. But in the past few years, the concept of corporate social responsibility—increasingly part of the curriculum in America's schools of business and management—has established itself as a political and social force to be reckoned with. This can be seen in recent proposals in Congress and elsewhere to offer tax breaks or regulate differently firms that shoulder their "social responsibilities."

Another sign of the increasing prominence of the idea was the formation of Business for Social Responsibility (BSR) in Washington, D.C., in 1992. The 54 founding members of BSR—including Ben & Jerry's Homemade, Inc., The Body Shop, Stride Rite Corp., and Working Assets—were well known as advocates of environmentalism and economic "fairness." The organization said it intended, through lobbying and public relations, to make "social equity," "environmental responsibility," and "developing a sustainable economy" integral to corporate decision-making. BSR now has more than 800 members and affiliates, including AT&T, Federal Express, Hallmark, and Time Warner.

Social responsibility isn't expected only of large corporations. If commercial activities are perceived to be unethical or destructive, it doesn't matter what type of business enterprise engages in them. However, publicly traded corporations are the target of most discussion about social responsibility because of how they are created and managed.

Corporate social-responsibility advocates note that since corporations are "fictitious persons," created by law and sustained by government grants of limited liability for individual shareholders, they have obligations to society that surpass those of sole proprietorships or partnerships. One such scholar, business professor Thomas M. Jones of the University of Washington in Seattle, explained that "the corporation which acts in a responsible manner may simply be paying society back for the social costs of doing business, costs for which the firms rarely receive an invoice."

This view is hardly new. In fact, it was accepted doctrine in the United States and other Western societies until the nineteenth century that the right to conduct business in the corporate form was a matter of royal or state prerogative, not of private economic interest. Monarchs issued charters to public-stock corporations that promised public benefits, such as exploration and colonization of the New World. Individuals could own shares of the corporation, and sell them (with some

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limitations), but the purpose was not merely to serve the interests of stockholders. In the American colonies, the earliest business corporations established during the eighteenth century were founded to perform such services as building transportation infrastructure, supplying water, fighting fires, and providing insurance. These early corporations were rare and closely regulated in size, scope, and property holdings.

Self-Incorporation Permitted

After the break from England, however, American states began to pass charters that allowed self-incorporation rather than incorporation by special legislative act. At first, these corporations could be created only for religious, charitable, or municipal functions. The first private incorporation statute, passed by the North Carolina state legislature in 1795, applied only to canal builders, and the canals had to pass to state ownership. Later, however, states broadened the scope of self-incorporation to the point where firms began to arise throughout the economy for the clear purpose of conducting private business.

At the turn of the century, the implicit assumption underlying state corporate law was that the corporation existed to make money for its shareholders. This consensus was rarely challenged. The first important legal test of the responsibilities of corporate directors came in the influential 1919 case of *Dodge v. Ford*. Despite its name, the case had nothing to do with competition between automakers. Instead, it had to do with the intended largess of Henry Ford, president and controlling shareholder of the Ford Motor Company. In August 1916 Ford owned 58 percent of company stock. John and Horace Dodge owned 10 percent. Rather than pay regular and special dividends, as the company had done in previous years, Ford announced that only regular dividends would be paid. The remaining profits would be used to expand production capacity, increase wages, and offset losses expected from his cutting the price of cars.

Many analysts have interpreted Henry Ford's strategy as an astute business decision calculated to increase profits in the longer run. But that wasn't his stated purpose. Ford proclaimed broader social goals: "to employ still more men, to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes." The Dodge brothers sued, claiming that Ford was using shareholder equity to pursue his own personal philanthropic goals. The Michigan Supreme Court, while professing to respect Ford's business judgment, agreed with the Dodges. It stated that a corporation exists to benefit its stockholders and that corporate directors have discretion only in the means to achieve that goal. It may not use profits for "other purposes."

The court went on to say that corporate behavior such as charitable giving could pass legal scrutiny as long as it had a legitimate relationship to corporate profits. Other state courts codified this standard by upholding corporate expenditures such as gifts to local training schools, community chests, recreational facilities, hospitals, and even churches. Expenditures designed to attract customers and advance corporate interests by obtaining "good will and prestige" also passed muster.

As a practical matter, then, *Dodge v. Ford* and similar cases throughout the early twentieth century gave corporate managers great discretion. Nevertheless, the case did establish in the minds of corporate managers and others the notion that corporations had direct responsibilities only to shareholders.

Principle Under Fire

After the Great Depression hit and throughout the war years, this notion came under fire from several fronts. First, a number of scholars and observers of business came to advance the proposition that corporations, far from being owned and thus controlled by their shareholders, were really accountable to no one but their managers. Adolf Berle and Gardiner Means, in their influential work, *The Modern Corporation and Private Property,* argued that shareholders were passive owners at best; they effectively exercised only the power to sell their shares if dissatisfied with

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corporate policies or performance. "By surrendering control and responsibility," Berle and Means wrote, shareholders had "surrendered the right that the corporation should be operated in their sole interest." Their book, published the same month Franklin Roosevelt was elected, helped justify the economic regulations imposed in the early New Deal.

Another argument advanced was that corporations had grown so large and amassed so much power over society that previous formulations of their social responsibilities had simply become outdated. This view was stated by the New Jersey Supreme Court in *A.P. Smith Manufacturing Co. v. Barlow*, the 1953 case that helped redefine the purpose of corporations in the minds of many executives, judges, and scholars. In 1951, the board of directors of A.P. Smith, a manufacturer of valves and fire hydrants, adopted a resolution to contribute $1,500 to Princeton University. Corporate shareholders challenged the donation as being outside the proper scope of corporate expenditure. The court disagreed and upheld the contribution. Harking back to the royal charters, the court said that the shareholders, "whose private interests rest entirely upon the well-being of the corporation, ought not to be permitted to close their eyes to present-day realities and thwart the long-visioned corporate action in recognizing and voluntarily discharging its high obligations as a constituent of our modern social structure."

Around the same time, other court decisions and new state statutes recognized the power of corporations to make donations to the public welfare or for charitable, scientific, or educational purposes. Advocates of corporate social responsibility began to argue that if philanthropy was a legitimate corporate activity, then perhaps other activities that placed social goals over shareholder returns were also legitimate, such as abandoning profitable but (in their view) socially or environmentally destructive product lines. The actual legal status of corporate social responsibility probably did not change a great deal between *Dodge v. Ford* and *Smith v. Barlow*, since managers had always enjoyed a substantial amount of discretion in how to serve what they perceived to be the economic interest of the corporation. But in *Smith*, the court, along with other legal and academic commentators, suggested that the corporate interest itself had changed. Because they controlled institutions of economic power and social influence, responsible corporate managers (as well as government regulators), according to this outlook, should consider a host of goals other than profit maximization.

Reaction and Counteraction

Many business leaders and academics viewed the corporate social responsibility movement with alarm. To them, it went hand in hand with increased government control over private economic decisions. The most famous critic is Nobel laureate Milton Friedman, author of *Capitalism and Freedom*. Friedman, while teaching at the University of Chicago, wrote perhaps the most widely cited—and criticized—essay on corporate social responsibility in the past 30 years: "The Social Responsibility of Business Is to Increase Its Profits." In that modest five-page article in the September 13, 1970, issue of the *New York Times Magazine*, Friedman sought to clarify the legal and ethical issues involved in the debate by noting that businesses are simply groups of people and that only people have responsibilities. If a corporation makes a donation to charity without the shareholders' authorization, wrote Friedman, the managers are deciding how to spend other people's money. It would be better to return the money to shareholders as dividends or capital gains and let them decide which charities to support.

In Friedman's view, the purpose of the corporation is clear: "There is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud."

It is no exaggeration to say that, with very few exceptions, every major article on or analysis of corporate social responsibility since the publication of Friedman's article has cited, mentioned, or challenged it. Some critics maintain that Friedman's understanding of corporate ownership is badly dated. Since

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shareholders are passive or even unknowing investors in particular companies (through pension or mutual funds), they don't exercise the type of control that real owners of property do. "With the dissolution of ownership in the traditional sense," wrote Michigan State University legal scholar Jeffrey Nesteruk in the *Cincinnati Law Review*, "the dichotomy between shareholder and societal member must be reconsidered." Another argument lodged against Friedman's view is that dividing profit-seeking business activity from the larger world of political, legal, and social decision-making is impossible. "Role specialization, which perhaps is desirable, does not and cannot exist in our modern industrial economy," Thomas Jones stated. "Corporations play a political role; governments play an economic role. Profit alone no longer implies preferred behavior. . . . Corporations are social institutions and as such must live up to society's standards; society has changed the standards for corporations, as it has every right to do."

Friedman has responded that social changes have not invalidated the distinction between corporations and other institutions. Nor is the relationship between shareholder and corporate manager anything but an owner-employee, or principal-agent, relationship. To suggest otherwise is merely to substitute one's own judgment for the judgment of shareholders, who, after all, voluntarily decide whether or not to invest their funds. They (or their agents among money managers) will sell the stock of companies from which they no longer expect competitive returns. Indeed, the proliferation of stock ownership through institutional investors has merely reinforced the responsibility of corporate managers to focus like a laser beam on profit as an objective. Advocates of corporate social responsibility may not like the implications of this trend, but that does not justify their attempts to second-guess shareholders in their wish for an economic return.

Shifting the Debate

The debate over corporate social responsibility has focused on such issues as the nature of corporate ownership in America today and the legal or fiduciary responsibilities of corporate managers in business transactions such as takeovers and mergers. But there remain a couple of points from Friedman's discussion that are unappreciated.

One is the important notion that corporations do not exist in physical reality. This has implications beyond Friedman's contention that corporations, as artificial persons, cannot really have social responsibilities. Consider that corporations consist of more than simply their land, plants, machinery, inventory, and products. The value of a corporation—at least in the minds of those who buy, hold, or sell its stock—is based on both tangible and intangible assets. A company with few assets today but a great idea for a new product may dominate the marketplace tomorrow, while a company with millions of dollars in assets and a large market share in a soon-to-be obsolete industry may be destined for failure. Hard-to-quantify characteristics, such as worker morale, management style, systems for promoting internal innovation, and an ability to foresee future trends, determine the expected value of corporate stock.

Can individual shareholders really be viewed as "owners" of such corporate assets as the brainpower and work ethic of employees, or the goodwill and confidence of consumers? A more meaningful way to think about corporations may be that they are bundles of ever-changing and variably valuable private agreements between individual persons. Coca-Cola, for example, might be reasonably thought of as a set of bilateral and multilateral agreements between such groups as farmers, factory workers, plastic designers, bauxite miners, graphic artists, bankers, bond buyers, managers, retailers, soda drinkers, and celebrity spokesmen. All these individuals (and many others) enter into contracts with Coca-Cola in which they agree to provide something of value in exchange for something else of value.

Stockholders are no different; they agree to risk their wealth as equity owners of the corporation in exchange for a shot at a profitable return on their investment. There is nothing socially undesirable about this emphasis on profit. Many American families rely on invest-

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ments in stocks or mutual funds to make the down payment on their first home, to send their kids to college, or to live decently in retirement. Shareholders of U.S. corporations seek profit in the same way that other groups of Americans seek higher wages as workers, higher interest rates as lenders, lower interest rates as borrowers, and lower prices as consumers. Corporations serve as the venue where these sometimes compatible, sometimes competing interests are accommodated in ever-changing, but always mutually satisfactory ways.

Stephen Bainbridge of the University of Illinois College of Law has suggested that this "nexus of contracts" view of corporations establishes a firmer defense of profit as the goal of corporations than the traditional understanding of shareholder "ownership" that Friedman employs. After all, shareholders of publicly traded companies differ from, say, homeowners in some easily recognizable ways. Someone who buys a few shares in Coca-Cola and is subsequently caught breaking into a bottling plant cannot defend himself by proclaiming that since he is an "owner" of Coca-Cola, he has a perfect right to enter.

Thinking of the responsibility of managers to stockholders as stemming from a contract with a specified goal—the maximization of the return on investment—might be more helpful than thinking about property ownership per se. By embracing the contractual definition of a corporation, Bainbridge is able to argue that state laws allowing incorporation are not special public favors to shareholders, justifying imposition of social obligations. Instead, they are merely "default rules" for establishing contracts between buyers and sellers of equity that would come about in the marketplace anyway, but at a high transaction cost. Rather than having every corporation and potential shareholder negotiate and sign contracts, the law recognizes a baseline corporate contract that everyone is presumed to agree to unless otherwise specified. "Refusing to hold shareholders personally liable for firm debts thus is the precise equivalent of enforcing a standard form sales contract, nothing more and nothing less," Bainbridge contends.

Profit and the Common Good

Another of Friedman's points that deserve greater attention is his suggestion that "the people who preach the doctrine of social responsibility are concealing something: the great virtue of the private enterprise system is precisely that by maximizing corporate profits, corporate executives contribute far more to the social welfare than they do by spending stockholders' money on what they as individuals regard as worthwhile activity." Here is the crux of the matter. The assumption that profit is inconsistent with the common good is predicated on a perceived tension between making money and serving one's fellow man. But as Adam Smith said centuries ago, if the pursuit of profit really does act as "an invisible hand" guiding human action toward socially beneficial endeavors, then surely to abandon that pursuit is to lose the social benefits that would otherwise exist.

In other words, perhaps commercial activity—as distinguished from other forms of behavior, such as personal philanthropy or government action—confers unique benefits on society. Realistically, all sorts of problems in society can be viewed as within the purview of corporate activity. But in Friedman's view, the response of corporations to these problems will and must be different because of the nature of profit-seeking business. "The crucial question for a corporation is not whether some action is in the interest of the corporation, but whether it is enough in its interest to justify the money spent," he wrote. Companies, then, bring a search for efficiency and economy to the task of solving problems. This search represents a fundamentally different way of addressing social problems from the means employed by governments, charities, churches, or families. To erase the distinctions between corporations and other institutions is potentially to lose the unique problem-solving opportunities that free enterprise creates. In effect, private business is fulfilling its "social responsibility" if, and only if, it tries to make a profit. □

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THE FREEMAN
Ideas On Liberty

"49 and Holding"

by Raymond J. Keating

The federal regulatory monster inflicts massive costs on the U.S. economy. No sector feels this statist wrath more sharply than small business.

Perhaps burdened the most are small, enterprising firms looking to expand. Like the federal progressive income tax, many regulations punish success: a growing firm that adds employees faces an ever-increasing regulatory burden. Indeed, the incentives to stay small are considerable.

While placing hard numbers on the burdens government imposes on the economy and predicting future burdens are dicey endeavors, the following sobering estimates are worth noting. In a 1996 study, economist Thomas Hopkins projected that the total cost of federal regulations would be $700 billion for 1998, measured in 1995 dollars.[1] That represents a real increase of 28 percent over the recent low of $549 billion a decade ago in 1988. Of course, regulatory costs fall hardest on smaller enterprises. Estimated per employee, costs for firms with fewer than 20 employees run 86 percent higher than those for businesses topping the 500-employee mark. Firms with 20 to 499 employers have costs 78 percent higher than larger companies.[2]

However, as *The Economist* magazine noted in its July 27, 1996, issue, Hopkins's projections were "conservative." For example, they did not include federal regulatory enforcement spending, which, at the very least, approaches $20 billion annually. Also, according to the magazine, Hopkins's figures "include only the burden of complying with rules for which cost studies have been done. Some costs, such as the loss of productivity caused when new regulation forces firms to adjust, are left out altogether."

Lost Productivity

Economist Richard Vedder estimated that federal regulatory activity from 1963 through 1993 reduced productivity growth by one percentage point annually, meaning that GDP in 1993 would have been $7.614 trillion instead of $6.343 trillion.[3] That's a $1.27 trillion loss in economic output due to increased federal regulatory activity—in addition to compliance costs and federal spending.

In 1992, analysts Nancy Boyd and William Laffer III estimated that total federal and state net regulatory costs (after accounting for the so-called benefits of regulation) registered upwards of $1.7 trillion annually.[4] Laffer further estimated that lost GDP growth due to excessive regulation over the previous two decades led to an absence of 3.6 million to 9.6 million jobs that would have been created.[5]

Make no mistake, small to mid-sized businesses are the primary engine of job creation in the economy, accounting for anywhere from two-thirds to more than 100 percent of *net* jobs created in any particular year.

Raymond Keating is chief economist at the Small Business Survival Foundation, a columnist with Newsday, and a contributing editor of The Freeman.

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According to an analysis performed for the Small Business Administration, firms with fewer than 500 employees in 1992 created almost 12 million new jobs by the close of 1996. By contrast, firms with more than 500 employees in 1992 wound up losing 645,000 jobs by 1996. Therefore, since the burdens of regulation fall heaviest on small businesses, the impact of regulatory costs on employment is bound to be severe.

Bogus Relief

To reduce the regulatory burden, over the years Congress has exempted many businesses from certain regulations based on the number of employees. Regulations take effect at thresholds ranging from 10 to 100 workers.

Unfortunately, this is another example of good intentions gone awry. Quite simply, as a firm grows and adds employees, it is subject to new regulations and therefore higher costs. For the small business content to stay quite small, exemptions may work in their favor (though they will still be hurt, as we all are, by regulation's overall damage done to the economy). However, for businesses seeking to grow, formidable additional costs are imposed as new regulations kick in. Any business considering expansion must ask if the increased regulatory costs of hiring more people outweigh the added profit made possible by the new employees? In the language of economics, does the marginal cost of labor now exceed the marginal revenue product? If so, new employees will not be added.

For many businesses, it makes sense to apply the brakes and stop growing. Indeed, for some, it actually may pay to get rid of some employees to avoid being hit by new regulations. A study by Congress's Joint Economic Committee estimated that under the Family and Medical Leave Act, which takes effect at 50 employees, a firm with 60 workers could increase profits by cutting back to 49.[6]

There are many anecdotes about companies cutting off expansion after reaching the threshold at which additional regulations take effect. Senator Robert Bennett reported an encounter with a businesswoman who said her company was at "49 and holding." She had no plans to hire more workers, because of the new regulatory burden that would follow. "If we didn't have the regulatory overhang that comes with 50 employees," she told the senator, "I could hire an additional five, seven, or ten people. I could do it tomorrow. But I'm not going to. We are 49 and holding. I know a lot of businesses in the same circumstance."[7]

The *Wall Street Journal* reported in 1993 that a Pittsburgh company that processes flat-rolled steel coils increased its work force to 49 and then stopped to avoid the clutches of the Family and Medical Leave Act. A letter to the *Washington Times* in 1992 told of a Virginia instrument company that kept employment below 50 to avoid having annually to submit paperwork related to nondiscrimination in hiring; one company that exceeded 50 had submitted a file weighing more than eight pounds.

Is There a Solution?

As an answer to this threshold problem, regulation enthusiasts would extend the rules to small business. But spreading the economic damage makes no sense if one is concerned about the state of small business and the society's economic well-being.

Another option is to lift the bar even higher—say, to 250 or 500 employees. That would exempt more businesses, but growth-oriented companies would still find themselves stifled.

The only real answer is deregulation. The imposition of new regulatory burdens on all businesses should be stopped, and existing onerous regulations should be repealed. Most are simply unwarranted meddling in the marketplace. The government must get out of the way. □

1. Thomas D. Hopkins, "Regulatory Costs in Profile," Center for the Study of American Business, Washington University, St. Louis, August 1996.
2. Ibid.
3. Richard K. Vedder, "Federal Regulation's Impact on the Productivity Slowdown: A Trillion-Dollar Drag," Center for the Study of American Business, Washington University, St. Louis, July 1996.
4. William G. Laffer III, "How Regulation Is Destroying American Jobs," *Backgrounder* #926, Heritage Foundation, Washington, D.C., February 16, 1993.
5. Ibid.
6. Joint Economic Committee, "Derailing the Small Business Job Express," United States Congress, November 7, 1992.
7. Quoted in "Isn't Anybody Back There Listening?," *Inc.*, October 1993.

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Economics

Price Ceilings Cause Shortages and Higher Costs

The coordination of demand and supply, which we discussed last month, does not occur automatically. It is an example of Adam Smith's invisible hand, which leads people interested only in pursuing their own interests to make choices that promote the interests of others as well. But the invisible hand, as amazing as it is, works only under certain conditions. Without property rights, a defense against the violation of those rights from both external and internal threats, a predictable judiciary, a stable monetary system, and a limited government, the voluntary exchange on which social coordination depends quickly breaks down.

Government has important roles in protecting private property, preventing capricious judicial decisions, and protecting the monetary unit against debasement. But these functions can be performed effectively only by a limited government. Once government goes beyond protecting voluntary exchange as an impartial referee and attempts to determine particular outcomes, it disrupts the social cooperation that is the surest means to generally desirable outcomes. Examples of disruptive government incursions into market activity are unfortunately frequent. A particularly harmful form of government meddling is the attempt to outlaw market prices.

When most people think of market prices they don't think of the communication and cooperation those prices allow. Consumers typically see prices as too high and therefore an impediment to their desire for more things. Suppliers see the same prices as too low. What happens when the government responds to consumer pressures by imposing a maximum legal price on a product below the price the market would set? The unfortunate, and ironic, result of a price ceiling is to increase the cost of products to consumers.

In the accompanying figure the demand curve, D, and supply curve, S, determine a price P*, which the market tends toward. As I discussed in last month's column, P* motivates suppliers to make available exactly that amount, Q*, that consumers want at that price. This ability of millions of people to coordinate their decisions with one another is the result of the information they communicate through market prices. Now consider what happens when the government imposes a price ceiling below P*, say at P_C.

At that price suppliers are willing to make available only Q_S units of the product, while consumers are anxious to buy Q_D units. The result is a shortage, as consumers cannot get as much of the product as they want. Shortage—the inability to buy a product although one has the money in hand—is different from scarcity, which we can define as the inability of people to have as much as they would like at a zero price. Scarcity is an unavoidable feature of the real world; shortages are not. Any shortage would be eliminated by the price generated by market communication, so shortages are always created by government restrictions on market prices.

Dwight Lee is Ramsey Professor of Economics and Private Enterprise at the University of Georgia.

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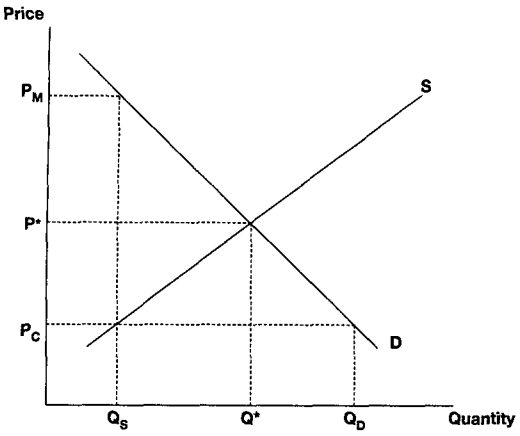

Advocates of price ceilings claim that they lower the cost of the product for consumers. This claim seems plausible since the price consumers pay is P_C after the ceiling is imposed instead of P*. But you can't lower the cost to consumers by restricting the price communication that allows them to secure the maximum cooperation from suppliers. Indeed, price ceilings increase the consumers' cost. Since the height of the demand curve tells us how much consumers are willing to pay for another unit of the product, we can see from the figure that when only Q_S units of the product are available, consumers are willing to pay Pm rather than do without. And just because they can't legally pay that amount in dollars doesn't mean they won't pay it in other ways.

For example, one way consumers compete during shortages is on the basis of first-come, first-served. According to Hedrick Smith's book *The Russians*, the average housewife in the former Soviet Union spent 14 hours a week queuing up for products because of the shortages created by pervasive price ceilings. How long will people queue up for an additional unit of a price-controlled product? Until the cost of doing so is equal to the difference between what they are willing to pay, P_M, and the price ceiling, P_C. So the total monetary and time cost will tend toward Pm, which is more than consumers would pay without the price ceiling. The consumers pay more, but notice, the suppliers don't receive more. The higher amount consumers pay does nothing to communicate to suppliers that more should be made available.

Another common cost-increasing response to price ceilings is reduced quality. While suppliers cannot legally benefit from the excess demand (Q_D - Q_S) by raising the price above P_C, they can reduce the quality of the product, which reduces their costs. The reduction in quality can take many forms, and is often tied in with the queuing just discussed.

Rent controls cause a deterioration in the quality of apartments. When landlords have more demand than they can satisfy, and are unable legally to charge higher rents, they reduce costs by doing less to maintain their apartments. New York City once tried to solve this problem with its rent-control law by exempting tenants from paying the rent if their apartments were damaged. Not surprisingly, tenants began breaking windows and ripping up carpets to avoid paying the rent.

Of course, some consumers come out ahead under price ceilings. With lots of people anxious to buy at the controlled price, it doesn't cost suppliers much to discriminate against certain people. Those whom suppliers favor often get products at lower prices without long waits. For example, celebrities and the politically well-connected have no trouble obtaining rent-controlled apartments in New York City, while others end up doing without.

But most consumers are harmed by price ceilings. This is hardly surprising since price ceilings prevent consumers from communicating with suppliers in ways that motivate the best possible response to their demands. □

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THE FREEMAN
Ideas On Liberty

"Wrecking": The Ominous Rationale for Attacks on the Tobacco Industry

by Daniel Hager

The state of Minnesota's lawsuit against the tobacco industry has ended in a multi-billion-dollar settlement. Litigation by other states is expected to yield them lucrative windfalls as well, and Congress has had its own eye on forcing the industry to capitulate to its demands.

In the wake of Minnesota's triumph, the Associated Press quoted state Attorney General Hubert Humphrey III as saying, "Today the tobacco industry has surrendered, and they have surrendered on our terms." But before he and other members of the anti-tobacco forces become over-jubilant, they should examine the ramifications of their actions.

With the tobacco industry's loss of constitutional protections, the government's philosophical justification for its assault is clearly collectivist. As in the Soviet Union 70 years ago, the rationale for wanton attack is simply that the accused is a "wrecker," culpable for damaging the collective. In the absence of due process, anybody is vulnerable to being found guilty of "wrecking activities."

Whose Money Is It?

To extract monetary penalties from the tobacco industry, Humphrey and the other judicial and legislative adversaries have to apply the dubious collectivist principle that governments own the money they spend. Minnesota and other states claim that their Medicaid expenditures for individuals allegedly injured by smoking "cost" these governmental bodies a certain amount of money and that they are therefore entitled to recover it from the alleged culprits.

However, there is no actual cost to governments because they have a custodial rather than ownership role with respect to the taxpayers' money. Governments take money from some and distribute it to others, who become beneficiaries. The beneficiaries receive as much as the governments disburse, so the costs are canceled out by those gains.

If the tobacco industry caused the state government to pay medical costs of some Minnesotans (those who smoked and received state aid), then the industry also created benefits for Minnesota's doctors, nurses, and ancillary medical staff, as well as a sizable bureaucracy to administer associated paperwork. In addition, any such illnesses enabled Minnesota's hospitals and nursing homes to increase their occupancy rates and thereby contributed to their economic health. A heightened demand for rooms may even have prompted the building of new facilities, a boon to the construction industry and its employees. In other words, when government

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intervenes as a third-party payer, illness becomes a form of public works, ranking alongside projects like government-funded buildings, roads, bridges, sports facilities, and so forth.

Thus the current tobacco controversy reduces itself fundamentally to an exercise in interventionist public-works theory. Government spending on public works is sometimes justified on the grounds that it stimulates the economy and creates jobs. Under that theory, the purported transgressions of the tobacco industry have had a salubrious stimulative economic effect. The irony of collectivist and quasi-collectivist systems is that illness is like public works. Curious, is it not, that the tobacco industry is blamed for the costs but not credited for the benefits.

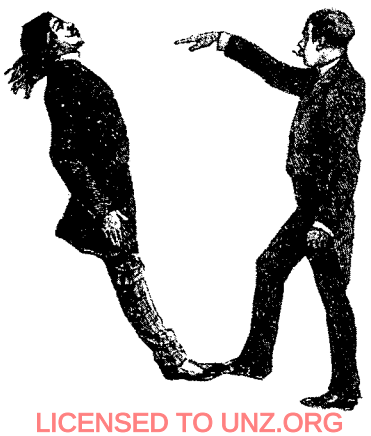
What the present controversy swirling around tobacco actually elucidates is that the fundamental problem is not the industry but state intervention, which distorts issues of culpability and redress and expands the level of public works.

Advocates of public-works expansion should be directed to the works of French economic analyst Frederic Bastiat, who demolished their arguments a century-and-a-half ago. In *Essays on Political Economy*, Bastiat wrote: "The great Napoleon, it is said, thought he was doing a very philanthropic work by causing ditches to be made and then filled up. He said, therefore, 'What signifies the result? All we want is to see wealth spread among the labouring classes.'"

But the wealth is chimeric: "While you state the destination given by the State to the millions [of francs] voted, do not neglect to state also the destination which the tax-payer would have given, but cannot now give, to the same. Then you will understand that a public enterprise is a coin with two sides. Upon one is engraved a labourer at work, with this device, *that which is seen;* on the other is a labourer out of work, with the device, *that which is not seen."* (Italics in original.) When individuals spend in their own interest, markets respond, and greater wealth is generated than when their money is siphoned off to pay for something the state represents as being for the collective good. When societies are organized for the furtherance of an ostensible collective good, dire results are not unexpected. Individual rights are abrogated, and a ruling caste emerges to define what constitutes that public good. Public expenditures must be kept to a bare minimum.

The abuse of power by government in attacking the tobacco industry differs from the conduct of the Soviet Union of 1930 only in degree. The *Piatiletka,* Stalin's five-year economic plan initiated in 1928, collapsed in chaos, and expediency dictated that scapegoats be identified and punished as "wreckers" of the proletariat. In the case of the state fisheries, scientists who had been conscripted into managerial positions, most of them apolitical, were singled out and punished.

On one level the tobacco spectacle is playing out simply as the machinations of ambitious politicians and lawyers using extortionary tactics to achieve their own ends. But since constitutional restraints on government power have been ominously rescinded in favor of collectivist principles, nobody is safe. □



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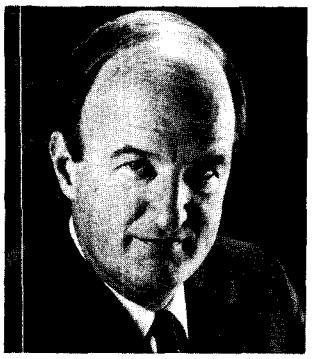
THE FREEMAN
Ideas On Liberty
NOVEMBER 1998



A Golden Comeback, Part III

"A free gold market . . . reflects and measures the extent of the lack of confidence in the domestic currency."
—LUDWIG VON MISES

In the past two columns, I've highlighted the uses and misuses of gold. Despite occasional calls for a return to a gold standard, the Midas metal has largely lost out to hard currencies as a preferred monetary unit and monetary reserve. Most central banks are selling gold.

Gold has also done poorly as a crisis hedge lately. It has not rallied much during recent wars and international incidents. U.S. Treasury securities and hard currencies such as the German mark and Swiss franc have become the investments of choice in a flight to safety.

Nor has gold functioned well as an inflation hedge over the past two decades. The cost of living continues to increase around the world, yet the price of gold has fallen from $800 an ounce in 1980 to under $300 today.

What's left for the yellow metal? I see two essential functions for gold: first, a profitable investment when general prices accelerate and, second, an important barometer of future price inflation and interest rates.

Dr. Skousen (http://www.mskousen.com; mskousen @aol.com) is an economist at Rollins College, Department of Economics, Winter Park, Florida 32789, a Forbes *columnist, and editor of* Forecasts & Strategies. *He is also the author of* Economics of a Pure Gold Standard, *3rd Edition (Foundation for Economic Education, 1996). He is currently working on his own textbook,* Economic Logic.

Gold as a Profitable Investment

Since the United States went off the gold standard in 1971, gold bullion and gold mining shares have become well-known cyclical investments. The first graph demonstrates the volatile nature of gold and mining stocks, with mining shares tending to fluctuate more than gold itself. The gold industry can provide superior profits during an uptrend, and heavy losses during a downtrend.

One of the reasons for the high volatility of mining shares is their distance from final consumption. Mining represents the earliest stage of production and is extremely capital intensive and responsive to changes in interest rates.[1]

Gold as a Forecaster

Gold also has the amazingly accurate ability to forecast the direction of the general price level and interest rates. In an earlier *Freeman* column (February 1997), I referred to an econometric model I ran with the assistance of John List, economist at the University of Central Florida. We tested three commodity indexes (Dow Jones Commodity Spot Index, crude oil, and gold) to determine which one best anticipated changes in the Consumer Price Index (CPI) since 1970. It turned out

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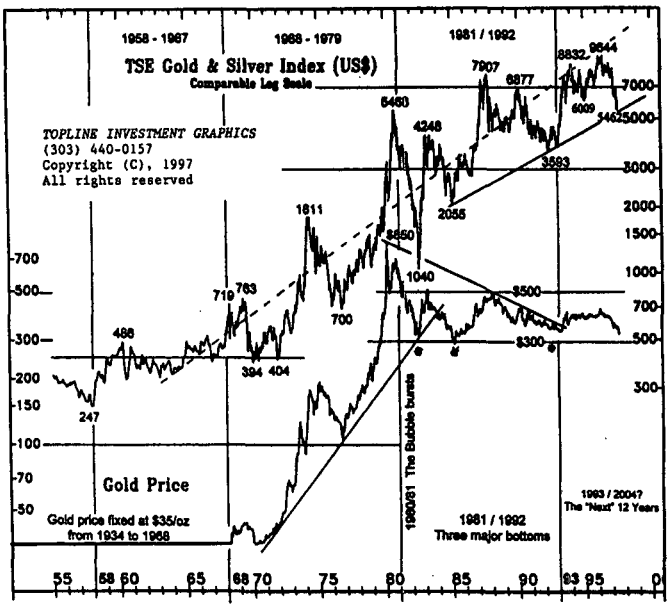
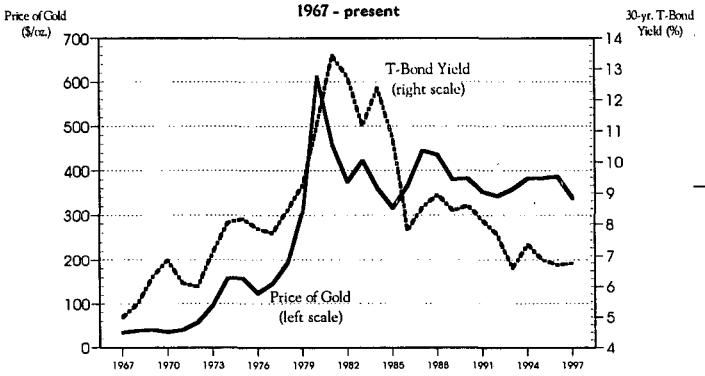


that gold proved to be the best indicator of future inflation as measured by the CPI. The lag period is about one year. That is, gold does a good job of predicting the direction of the CPI a year in advance. (All three indexes did a poor job of predicting changes in the CPI on a monthly basis.)

Richard M. Salsman, economist at H. C. Wainwright & Co. in Boston, has also done some important work linking the price of gold with interest rates. As the second graph demonstrates, the price of gold often anticipates changes in interest rates in the United States. As Salsman states, "A rising gold price presages higher bond yields; a falling price signals lower yields. . . . Gold predicts yields well precisely because it's a top-down measure. It is bought and sold based purely on inflation-deflation expectations; thus it's the purest barometer of changes in the value of the dollar generally."[2]

Figure Two

Gold Price and Treasury Bond Yields
1967 - present



In sum, if you want to know the future of inflation and interest rates, watch the gold traders at the New York Merc. If gold enters a sustained rise, watch out: higher inflation and interest rates may be on the way. □

1. For further discussion regarding the inherent volatility of the mining industry, see my work *The Structure of Production* (New York: New York University Press, 1990), pp. 290–94.

2. Richard M. Salsman, "Looking for Inflation in All the Wrong Places," *The Capitalist Perspective* (Boston: H. C. Wainwright & Co. Economics), October 15, 1997. For information on his services, call (800) 655–4020.

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BOOKS

Achieving Our Country
by Richard Rorty
Harvard University Press • 1998 • 159 pages
• $18.95

Reviewed by George C. Leef

Do leftists have anything new to say? Any interesting responses to the many arguments advocates of freedom have lodged against their coercive nostrums? Any novel socio-economic analysis to which we ought to pay attention? The only way to find out is to read them.

Richard Rorty is a proud, thoroughbred leftist (his parents were well-known socialists in the interwar and postwar years) and professor of humanities at the University of Virginia. This book is a collection of lectures centering on Rorty's conviction that the American left is no longer playing the role that it should in the nation's politics. He writes longingly of bygone years: "when an intellectual stepped back from his or her country and looked at it through skeptical eyes, the chances were that he or she was about to propose a new political initiative." Today, Rorty frets, the left is becoming "spectatorial."

Before taking up the question of whether the book contains anything freedom lovers ought to take note of, the absurdity of complaining that today's left is insufficiently political needs a response. There has certainly been no slackening of the torrent of leftist proposals for achieving *their* country. No, we haven't had anything as bold and exciting (to Rorty and his ilk) as Lyndon Johnson's Great Society recently, but that is mostly because the left now advances its control through the stealthy means of regulatory edicts and judicial rulings. They seldom make headlines, but they augment the power of the state just the same. Worrying that the left is becoming nonpolitical is just as silly as worrying about free-market monopolies, global warming, and other hobgoblins.

All right, so the premise behind the book is nonsensical. There is a lot more to it than that, and Rorty's writing gives us a good look at the leftist mind at work.

He complains that the old alliance between the intellectuals (to Rorty, leftists are *the* intellectuals) and the unions has broken down, thus impeding the realization of the goals so dear to his heart. Wise up, Professor Rorty. The unions were never really interested in the misty-eyed socialist vision. What unions have always wanted, as Samuel Gompers said, was simply "More." Union rhetoric on "justice" and "equality" may have taken in some ivory-tower types, but their agenda has and always will be narrowly self-interested. Rorty, incidentally, has no criticism for union-backed laws and regulations that drive up prices for poor people and restrict job opportunities.

Rorty also says that Marxism was bad in practice, but that was not due to any inherent flaw in the theory. "Had Kerensky managed to ship Lenin back to Zurich," he writes, "Marx would still have been honored as a brilliant political economist who foresaw how the rich would use industrialization to immiserate the poor." He drags out old warhorses such as the idea that capitalists use "the reserve army of the unemployed" to keep wages down to subsistence levels. We have more than two centuries of evidence that capitalism inevitably leads to rising real incomes for rich and poor, factory owner and janitor alike, but Rorty is among those people who say, "My mind is made up; don't confuse me with facts."

Clichés are generally a substitute for serious thought, and Rorty liberally sprinkles them throughout his lectures. He calls the left "the party of hope." Never mind that millions have fled countries ruled by that party, and young people in nations such as Sweden are more accurately labeled "bored" and "listless" than "hopeful."

The most annoying thing about this book, though, is that the author writes as if free-market intellectuals had never said anything in criticism of the socialistic notions of which he is so fond. Consider "social justice." The phrase is used repeatedly throughout the book, but never does Rorty acknowledge the

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writings, to cite only the most prominent critic of this vaporous locution, of F.A. Hayek. Hayek's *The Mirage of Social Justice* (volume 2 of *Law, Legislation, and Liberty)* was a devastating attack on the term "social justice," arguing that it does not and cannot have any meaning. If Rorty has ever read Hayek (or Mises, Rothbard, Nozick, or any other serious critic of welfare-state interventionism), there is no evidence of it here.

Rorty loves to imagine the political system riding in on a white horse to rectify all the world's injustices, but a large body of free-market analysis—public choice economics—says that this expectation is hopelessly naïve. Naturally, you find no reference to James Buchanan or any other public choicer in the book.

Leftists seal themselves off from criticism of their ideas. Marx set the standard, saying that anti-socialist ideas couldn't have any validity because they came from the class enemy. Rorty basks in the imagined glow of the wonders of leftist activism, oblivious to the fact that his intellectual adversaries long ago demonstrated that welfare-state interventionism is harmful to the very people he thinks he is saving. It's like a teenager insisting that Santa Claus exists.

So, to answer my original question: no, you won't find any new ideas or arguments in this book, testimony to the bankruptcy of leftist thought. □

George Leef, president of Patrick Henry Associates in Michigan, is book review editor of The Freeman.

The Future Once Happened Here: New York, D.C., L.A., and the Fate of America's Big Cities

by Fred Siegel

The Free Press • 1997 • 260 pages • $24.00

Reviewed by Sanford Ikeda

There are many ways to tell the story of urban-policy failure. Economists have shown how rent control creates housing shortages, sociologists how welfare programs destroy poor communities, and urbanologists how urban planning can debilitate cities. In his book *The Future Once Happened Here*, historian Fred Siegel has added a new and insightful chronicle of modern liberalism's influence on social policy in New York, Washington, D.C., and Los Angeles over the last 30 years.

Siegel identifies racial tension as a main force that has driven urban policy since the 1960s. He lucidly and engagingly describes how that policy, informed by "riot ideology" based on liberal guilt and fear, transformed some major American cities from communities of tolerant strangers and great incubators of ethnic integration into rolling riots and sinkholes of federal largess.

Associated with the riot ideology is what Siegel terms "dependent individualism," the idea that each person has an absolute right to his "lifestyle," at public expense and regardless of the consequences for social cooperation. Those consequences have been a "moral deregulation of public space," which has eroded the trust that urbanologist Jane Jacobs identified as the lubricant that permits great cities to work well.

The largest part of the book is devoted to New York City. Siegel explains how Mayor Fiorello La Guardia's success in getting federal aid from FDR's New Deal in the 1930s set the pattern for fiscal irresponsibility in New York for the next five decades. Consequently, New York became dependent on an artificial, make-work economy, based on federally funded jobs and welfare bolstered by dependent individualism and the riot ideology. Nevertheless, its productive sector was still so large that both New York City and the state of New York have regularly sent more taxes to Washington than they have received in transfers. Surprisingly, supporters of big New York government appear blithely unaware of this fact.

Siegel sees hope in the evident success of Mayor Rudolph Giuliani's administration in New York in promoting public security by enforcing higher standards of public behavior. Less tolerance of "quality of life" crimes, such as loud car stereos and prostitution, seems to discourage the incidence of more serious crimes. As in Los Angeles, however, giving greater power to the New York Police

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Department may also have had its price.

The sections on Washington and L.A. are also illuminating. The peculiar nature of Washington's governance, which until recently lacked home rule, left it with no political tradition save for that of its notorious race-baiting mayor, Marion Barry. The pervasive federal presence has stifled the growth of the trust and informal organizations that mediate between citizens and their government, what social theorists now call "social capital." Thus, says Siegel, the morally and functionally bankrupt city of Washington appears to require solutions from the outside.

Siegel is somewhat more hopeful about Los Angeles. Siegel characterizes it as a city of energetic small entrepreneurs and flexible, decentralized government that has practiced less urban interventionism than New York or Washington. With its dispersed and diverse population, however, Siegel claims that L.A., like Washington, possesses little social capital. Nevertheless, he argues that its growing Latino population, with its relatively strong family and community structure and entrepreneurial spirit, is a cause for hope for the future even while language and cultural barriers remain sources of some present concern.

For those who would like to delve more deeply into the history of policy failure so readably presented here, the book's lack of references is frustrating. Nevertheless, Siegel has shown how good intentions, bad ideology, and what he calls "militant anti-consequentialism" can produce urban disaster. According to its perverse logic, "the devastation wrought by misguided politics was adduced as proof that even more money had to be spent on those same policies." He concludes: "Modern liberalism was born in the big cities and died there, a suicide of sorts. Liberals lost their birthright to govern big-city America not so much because they were overwhelmed by a well-armed foe but because their sense of moral superiority was so suffocating as to make it impossible for them to either adapt to new conditions or learn from their critics."

Milton Friedman, Nathan Glazer, and Jane Jacobs have each analyzed an aspect of the dynamics of what Ludwig von Mises termed interventionism, a process in which an intervention's unintended consequences only encourages further intervention. The process consists not in the isolated failures of regulation, welfare, or urban policy, but rather in their mutual interactions. While the definitive work on the dynamics of urban interventionism has yet to be written, Siegel's compelling book will deepen the reader's understanding of the turbulent forces that move great American cities. □

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Major League Losers: The Real Cost of Sports and Who's Paying For It

by Mark S. Rosentraub

Basic Books • 1997 • 513 pages • $27.50

Home Team: Professional Sports and the American Metropolis

by Michael N. Danielson

Princeton University Press • 1997 • 397 pages • $29.95

Reviewed by Raymond J. Keating

From the late 1980s into the first years of the 21st century, perhaps more than $15 billion will have been spent on new stadiums and arenas for teams in the four major league sports. Hundreds of millions of dollars more will have been expended for minor league facilities. On average, taxpayers foot at least 60 percent of the costs for major league venues and almost 100 percent for the minors.

This spending binge has resulted in a recent spate of books examining the politics and economics of professional sports. Leading the charge have been *Major League Losers* by Indiana University professor Mark S. Rosentraub and *Home Team* by Princeton University professor Michael N. Danielson. The final score on each is mixed at best, pleasing at times but ultimately unfulfilling and often frustrating—similar to watching a hockey game that ends in a tie.

In *Major League Losers*, Rosentraub is torn on the issue of taxpayer-financing of ballparks, stadiums, and arenas. He indignantly

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and accurately labels this a "welfare system." Rosentraub understands that subsidies pad the bottom lines of team owners, boost player salaries, and encourage owners to move their teams in search of bigger subsidies. No real economic benefits accrue to the cities.

His criticism of a sales-tax hike in Arlington, Texas, for the Rangers' new ballpark is on the mark: "It is still welfare in a state that abhors life on the dole; it is still a subsidy in a state that defends capitalism and the spirit of the free market." He also recognizes that sports are simply one part of a much wider entertainment industry: "Sports can provide entertainment, but so do movies, concerts, nature trails, bicycle paths and countless other activities." So far, so good. Unfortunately, *Major League Losers* is flush with statements and analysis flying directly in the face of such common sense.

For example, while Rosentraub denigrates this sports welfare system, he offers a multitude of suggestions on how governments can get better deals when undertaking such ventures, and even goes so far as to outline the best taxes for financing new facilities.

Rosentraub completely falters when he analyzes the St. Louis Blues' effort for a new arena. This section carries the subtitle "Saving the Blues: Doing Sports Right!!" According to Rosentraub, "doing sports right" means providing taxpayer subsidies, but not "excessive subsidies." Golly, the total taxpayer tab for the Blues' new hockey rink only came to $69 million, along with risk exposure on another $62.5 million in bonds. To the many people who are not interested in hockey, any subsidy is excessive.

Rosentraub's problem is that while he ably attacks the most egregious forms of sports welfare, at heart he favors industrial policy and so-called public-private partnerships. In his view, as long as the government has a plan and gets a piece of the pie, then it's okay for some taxpayer dollars to be used in building new sports facilities. Rosentraub calls this "municipal capitalism." Some of us still call it welfare.

Michael Danielson's *Home Team* amounts to a survey on the broader subject of professional sports teams and their relationships with cities, with primary emphasis on team movements and subsidies. Danielson writes well and provides a wealth of information and history on movements, stadium financing and lease deals, league structures, and revenue plans.

However, *Home Team* falters in the late innings as well. For one, the author displays an ignorance of market economics. He writes: "A market political economy legitimates private ownership of professional sports, promotes public investments in playing facilities that benefit private sports businesses and other powerful economic interests, and fosters aggregations of economic influence that often dominate the politics of professional sports." He's correct about private ownership rights, but fails to see that the other points have nothing to do with free markets.

From such a view of the market economy, Danielson then naturally offers little resistance to the sports welfare game. It's part of the system; he takes it as a given. So when addressing the idea of privatizing sports ventures, he is almost dismissive in tone, though offering little substantive criticism. For example, the author merely notes that team owners may not want to build their own stadiums (shocking!); that cities seeking teams may not wish to rely on private enterprise to get the job done; and that "almost all private arenas and stadiums built since World War II have involved significant governmental participation." Danielson does no more than point out the current state of affairs, offering no justification for the sports welfare system other than that team owners want it.

One of the most useful points made in *Home Team* is that in the early years of professional sports, government kept out: "In cities dominated by private enterprise, sports offered another opportunity for profit seeking. Teams were privately owned; they were organized into private leagues; and they played in private ballparks." Nothing in the book will convince the reader that we cannot and should not go back to the old days.

Both Rosentraub and Danielson largely place the blame for taxpayer subsidies on such misnomers as sports "cartels" or "monopolies," when in fact they are another

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outgrowth of our massive welfare state. Big government is alive and well in the wide world of sports. □

Raymond Keating is a contributing editor to The Freeman, *chief economist for the Small Business Survival Committee, and a columnist with* Newsday.

Unrugged Individualism: The Selfish Basis of Benevolence
by David Kelley
Institute for Objectivist Studies • 1996 • 65 pages • $9.95 paperback

Generosity: Virtue in Civil Society
by Tibor R. Machan
Cato Institute • 1998 • 116 pages • $8.95 paperback

Reviewed by Andrew I. Cohen

Critics often wonder how an ethics of self-interest has room for good will toward others, since it seems that egoism demands a ruthless unconcern for others. According to this caricature, egoists must cherish independence and eschew helping or being nice to other people. Is this position sound? Must egoists only growl at others?

Philosophers David Kelley and Tibor Machan each explore how an egoistic ethical theory not only permits benevolence but occasionally calls for it. Both authors cast benevolence as a key part of the good life. They argue that enlightened egoists cultivate good will as a means to personal enrichment.

David Kelley pays special attention to the role of benevolence in Ayn Rand's philosophy of Objectivism. Kelley sharply distinguishes benevolence from altruism. Benevolence is simply good will toward others; altruism, however, mistakenly holds that one's *duty* is to promote the interests of others, even over one's own interests.

In a world where mutually beneficial exchanges are possible, Kelley argues, benevolence is a form of showing respect for persons. He does not defend such respect by saying that we ought to promote another's welfare as an end in itself. Benevolence is instead a fitting public sign that you see others as possible values—material as well as spiritual—to yourself. Benevolence helps us "to exploit the potential represented by other people, to create opportunities for trade, to remake our social environment in the image of our values." Being sensitive, sympathetic, or generous, therefore, is a prudent investment with hopes of future returns.

While we can defend benevolence as a means to rationally selfish ends, some may be chilled by this picture of good will. One is benevolent, on this model, as a way of seeking some long-term payoff. This may be the selfish *justification* for benevolence, but it had better not be one's selfish *motive*. Persons who are benevolent as a means to an end will come off as scheming and insincere.

Suppose a friend supports another in a time of crisis. He might later explain his loyalty to his grateful friend by sincerely saying, "I just care about you." Alternatively, he might say, "I was hoping my being there for you would later pay off for me." Any healthy friendship must rest in some way on legitimate expectations of reciprocity. The authentically benevolent person, however, is not explicitly motivated by such factors. He shows good will to another because he *cares* about the other. While it is true that he cares about the other ultimately because doing so enhances his life in some way, he must treat the other's interests *as if* advancing them were an end in itself. Doing so is the best way of securing that long-term payoff.

Machan also sees generosity as a type of benevolence. In arguments Kelley would welcome, Machan claims that generosity is selfish (and virtuous) because it is part of "living successfully as a good human being." Machan argues extensively that prudent generosity best enhances one's ability to obtain goods from others in society.

His brief essay branches into many other topics: conceptions of self, negative versus positive rights, the moral significance of free will, the legitimacy of selling body parts, and the public policies that foster virtue. In all such wide-ranging discussions, Machan argues that individual sovereignty and private

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property are necessary for defining the freedom through which virtue is possible. Redistributing wealth or otherwise failing to take individual rights seriously curtails freedom and so restricts opportunities to be virtuous. At times Machan argues that virtue is *impossible* when individuals have no right to do wrong. Paying taxes, for instance, is not "generous," even if the money goes to a "worthy" cause. But a taxpayer may affirm in a spirit of generosity what the government has given him no choice but to do. Machan's analysis is strongest when he argues that virtue is *easier* where persons have the freedom not to do the right thing (as they do in free-market economies).

Machan and Kelley have each offered compelling, selfish justifications of good will to others. So long as egoists appreciate how to cultivate authentic virtue, they may stop squirming when asked why they are so nice. □

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Driving America:
Your Car, Your Government, Your Choice

by James D. Johnston

American Enterprise Institute Press • 1997 •
245 pages • $16.95

Reviewed by John Semmens

Driving America is a well-reasoned brief on behalf of the automobile. The car is the travel option of choice because it offers a fast, comfortable, convenient, and affordable way of getting where one wants to go. Nevertheless, there are those who would sacrifice this mobility on the environmental altar.

The crisis du jour is "global warming." The assumption is that the planet is getting warmer than it should be because of the environmentally "unfriendly" activities of humans. The most unfriendly human activity, according to Vice President Al Gore, is driving a car. Even "clean burning" auto engines emit carbon dioxide (CO_2). CO_2 is a greenhouse gas that helps trap heat from the sun on the planet's surface. We obviously need some global warming if life is to persist on the earth. The question is how much is enough? Environmentalists who have concluded that any more warming would be too much are seeking to reduce automobile emissions. But James D. Johnston, former General Motors vice president and a resident fellow at the American Enterprise Institute, contends that tightening emissions standards for automobiles is neither a necessary nor a cost-effective means of pursuing environmental goals.

One of the auto-emission programs he challenges is the Corporate Average Fuel Economy (CAFE) regulation. Initially the CAFE regulation was part of the Carter administration's energy conservation program. More recently, it has been adapted to an anti-greenhouse-gas agenda. Promoting better fuel efficiency doesn't sound like a bad idea—unless one considers the safety implications.

The main method by which vehicle manufacturers have complied with CAFE regulations has been to make cars smaller. Fuel has been conserved and emissions reduced. However, there has also been an increased risk to people in the cars. Each mile-per-gallon increase in fuel efficiency is correlated with a 3.9 percent increase in the fatality risk. This is because occupants of small cars are twice as likely to be killed in collisions as the occupants of large cars. Cars with wheelbase lengths of 114 inches or more have a 60 percent lower fatality rate than cars with wheelbases of 95 inches or less. To put this in perspective, the mandated air bag is estimated to reduce occupant fatality risk by 9 percent. Thus, the government's current proposal to make *all* cars smaller will likely increase the number of traffic fatalities. If safety is really our top priority, should we be trying to prevent people from buying large vehicles?

Consider the CO_2 emissions issue from an order-of-magnitude perspective. Globally there are over 150 billion tons of CO_2 emitted per year. Of this total, human sources contribute about 7 billion tons (less than 5 percent). All the cars in the United States contribute about 280 million tons. Consequently, even if every car in America were permanent-

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ly parked, annual global CO_2 emissions would be reduced by less than two-tenths of one percent. Obviously, it is unlikely that anything as drastic as a permanent ban on all auto travel will be enacted. So, the potential magnitude of impact from any politically feasible anti-auto measure would be extremely small.

The fact is, there is not much more room for environmental improvement to be had from efforts to mandate cleaner-burning engines, or restrictions on auto travel. Huge gains have already been achieved. Per-vehicle-mile carbon monoxide emissions are down 96 percent. Hydrocarbon emissions are down 97 percent. Nitrous oxide emissions are down 88 percent since the 1960s.

Rather than mandating new, lower standards, which may be infeasible or extremely costly, we need better enforcement of existing standards. The author reminds us that the worst 7 percent of emitters cause 50 percent of the pollution. Remedying this source of pollution through a mobile emission-testing program would be the most cost-effective way to make a significant reduction in vehicle-caused air pollution.

Johnston makes use of interesting historical statistics to illustrate that when it comes to pollution, the car is a substantial improvement over its predecessor. In 1900, horses in New York City "emitted" over 1,000 tons of manure and 70,000 gallons of urine per day. While these emissions are biodegradable, the health risks were considerably more immediate and pervasive than the risks posed by today's automobile emissions.

The book is a well-reasoned and carefully documented answer to the critics of the automobile. Its flaws are minor, springing from a "choose the lesser evil philosophy," which leads the author to support the "Partnership for a New Generation of Vehicles," a government-business endeavor.

Johnston urges those who appreciate the car to take political action on its behalf. Regardless of whether one follows this prescription, he offers a wealth of valuable information and insight for those interested in transportation and the environment. □

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Taxing Choice: The Predatory Politics of Fiscal Discrimination

Edited by William F. Shughart II

Transaction Books • 1997 • 411 pages • $39.95 cloth; $19.95 paperback

Reviewed by Roy E. Cordato

As faith in big government programs has waned in the past two decades so has the ability of the government to raise revenues through income-tax increases. Until recently, deficit spending has been the route around the public's resistance, but the people have caught on to that deception. What are revenue hungry congressmen and bureaucrats to do? The answer: give taxation a greater purpose. Use it as the weapon of righteousness against the forces of evil. Make it taxation, not to raise revenue, but to ward off the devil. The tax of the 2lst century is the sin tax or, more appropriately, the "choice tax."

Taxing Choice: The Predatory Politics of Fiscal Discrimination, edited by William Shughart, economics professor at the University of Mississippi, is a collection of essays that looks comprehensively at selective excise taxes through the lens of public choice theory, or what can be called the economics of interest-group politics. As Shughart points out, the argument for those taxes actually finds support in the economics literature. He writes in his introductory article, "The Economics of the Nanny State," that according to standard economic theory, an excise tax is justified when "the economic agents interacting in an unfettered market do not bear the full social costs . . . of their own decisions or choices. . . . [T]he consumption of certain products, such as alcohol and tobacco, imposes costs on society that the consumers do not themselves bear and which they consequently do not take into account when making decisions about how much to consume."

This quotation calls forth my one criticism of the book: it does not refute the theory of market failure and the case for social-cost taxes. In fact, the theoretical arguments against the theory are scarcely recognized by any of the authors.

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The book is divided into four sections, each covering a different aspect of the issue. Section 1, "The Political Economy of Excise Taxation," features three articles examining the economic "justification" for excise taxes and presenting a historical look at the use of these taxes in the United States.

Section II, "The Politics of Excise Taxation," examines how political decision-makers craft such taxes with an eye toward appeasing special-interest groups and diffusing taxpayer resistance. This section gets to the heart of public choice analysis. Professor Randy Holcombe states the premise: "arguments on both sides of the tax issue are almost always made by individuals who personally have something to gain from winning the argument. People choose to favor or oppose taxes based on the costs and benefits of the taxes *to them*." Thus, the crafting and implementation of the tax is a function of the political influence of the various winners and losers from the tax.

In addition, politicians are aware that they can buy their way to a new tax by earmarking revenues for popular causes—education, children's health care, for example. But as Dwight Lee points out in "Overcoming Taxpayer Resistance," money is fungible and new revenues from earmarked taxes simply free up other money. In other words, earmarking is simply a ruse to draw in supporters of the tax who might not otherwise have an interest in the issue.

The remaining two sections—"Alcohol, Tobacco, and Drugs" and "Constitutional Liberties and Excise Taxation"—are more case-orientated. Mark Thornton's "Prohibition: The Ultimate Tax" and Bruce Benson and David Rasmussen's "Predatory Public Financing and the War on Drugs: 1984-1989" are especially interesting. Benson and Rasmussen argue that even though illegal drugs cannot be directly taxed, the drug war is being driven by what amounts to a tax on illegal drugs, namely, asset forfeiture and confiscation. Indeed, the authors argue that what lured local law-enforcement agencies into accepting the Washington-driven "war on drugs" was the possibility of reaping some of these gains.

Professor Shughart and the Independent Institute are to be commended for assembling this collection of essays on what is likely to be the most important fiscal policy issue of the coming decades. □

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Hamilton's Republic: Readings in the American Democratic Nationalist Tradition

edited by Michael Lind

Free Press • 1997 • 345 pages • $25.00

Reviewed by David Upham

In this anthology, Michael Lind has compiled excerpts from speeches and writings by important American statesmen and intellectuals that are illustrative of what Lind calls the Hamiltonian or "Democratic Nationalist Tradition." Included among the Democratic Nationalists are such figures as Alexander Hamilton, Abraham Lincoln, Franklin Roosevelt, and Lyndon Johnson. Lind argues that they share a common attachment to four main political principles that distinguish them from their chief rivals, the "Jeffersonians": the primacy of the national community versus local communities; the sovereignty of the national people, rather than the sovereignty of the states; nationalist political realism instead of isolationism or world federalism; and a broad understanding of the powers and role of the federal government.

Lind clearly favors the Hamiltonian tradition, even going so far as to say that it is "the source of most of what is sensible and sound in American foreign policy, constitutional law, and economic policy." He confidently hopes for a revival of the Hamiltonianism (or at least his view thereof) most recently championed by New Deal and Cold War liberals and an end of the current domination (again in Lind's view) by the "Jeffersonian" conservative Republicans.

The chief and ruinous flaw in Lind's argument is that he ignores the fact that whatever

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the disagreements between Hamilton and the Federalists, on the one hand, and Jefferson and his allies, on the other, they were small compared to the divergence of opinion between all of the leading men of the Founding generation and the "Progressives" of the twentieth century. Hamilton, no less than Jefferson, would have repudiated the political projects of such Progressives as Herbert Croly and Franklin Roosevelt, whom Lind calls "Hamiltonian."

Lind can obfuscate the difference between Hamilton and the Progressives mainly because he presents only a few short excerpts from Hamilton's writings. In a 345-page anthology entitled *Hamilton's Republic,* one would expect to find more than 15 pages devoted to Hamilton's own work. Moreover, Lind presents these excerpts in a misleading way. For example, under the heading "The Need for Direct and Plenary Federal Authority," Lind includes a few passages from *The Federalist Papers*. Yet he fails to include those passages in which Hamilton emphatically states that the federal power is *not* plenary, such as insistence in *Federalist* 17 that if the federal government were to undertake to control "the administration of private justice between the citizens of the same State, the supervision of agriculture, and other concerns of a similar nature," it would represent "usurpations" of state authority.

While it is true that in opposition to Jefferson, Hamilton held that the federal government did have the constitutional power to establish a national bank, for instance, he would most certainly have opposed the recent establishment of a multitude of federal agencies to exercise extensive control over the details of economic and social life in the United States. Lyndon Johnson would hardly have agreed with Hamilton's statement at the New York ratifying convention that "whatever is not expressly given to the federal head is reserved to its members." Yet Lind calls Johnson one of the "greatest Hamiltonian presidents."

On a more fundamental theoretical level, what separates Lind's twentieth-century "Hamiltonians" from Hamilton and the rest of the Founders is their rejection of the earlier American consensus, according to which there is a universal, natural law from which one can derive fixed governing principles. In "The Farmer Refuted," another work Lind did not include, Hamilton (at the age of 18!) wrote that "the deity . . . has constituted an eternal and immutable law, which is, indispensably, obligatory upon all mankind, prior to any human institution whatever." According to this universal law, all men have certain rights, including the right to property: "no man had *any* moral power to deprive another of his life, limbs, property, or liberty." Legitimate government is instituted "for the security of [these] *absolute rights.*" This understanding of good government is, of course, virtually identical with that set forth in the Declaration of Independence. Franklin Roosevelt, Lyndon Johnson, and the others whom Lind praises saw things quite differently. □

David Upham is a doctoral student in political science at the University of Dallas.

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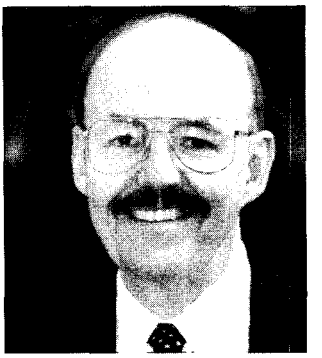

Paycheck Protection in California: What Went Wrong?

Proposition 226, which was on the primary ballot in California last June, would have required unions to get annual written permission from workers before spending their dues and agency fees on politics. The proposition lost 53 to 47 percent. In January, just after the initiative qualified for the ballot, polls indicated that over 70 percent of likely voters and a similar percentage of union households planned to vote for it. Exit polls on June 2 showed that 69 percent of the voters supported the idea of protecting paychecks against involuntary deductions for politics. John Sweeney, president of the AFL-CIO, called the outcome "a modern political miracle." As a proponent of the initiative, I have to ask what went wrong?

Opponents of 226, mainly unions, spent $30 million to defeat it, while supporters could muster only $3.5 million. Unions could take their money from dues and fee payers across the country. Supporters had to ask for donations. The opposition ran an intensive TV ad campaign three months before the first "Yes on 226" ad appeared. Early lies that went unanswered became established truths before the pro-initiative TV campaign began. In the final month before election day, opposition ads outnumbered proponents' ads by over 2 to 1.

The California business community gave almost nothing to support the "Yes on 226" campaign. Why? Two threats and one temptation. First, the unions collected signatures to put three initiatives on a later ballot that would increase the tax and regulatory burdens on businesses. Then they promised not to submit the signatures if the business community did not support 226. The unions proposed a Faustian bargain: let us continue to tax workers for politics and we will not increase your government-based headaches. This amounted to blackmail by ballot initiative, and too many businesses succumbed. It wouldn't surprise me if the unions submitted their signatures anyway.

Second, the unions threatened businesses with negative publicity campaigns asserting that employers who support 226 are anti-employee. Unions have discovered the efficacy of such efforts in their "corporate campaigns" against firms they seek to organize and firms they seek to punish for continuing to do business with strike targets. Well-intentioned but ill-informed members of the caring class—including clergymen, academics, and journalists—are often complicit in these efforts. And there are far too few business people, like T.J. Rodgers of Cypress Semiconductor, who dare to stand up and defend themselves against such unjustifiable attacks.

Third, many businesses believed they could get a free ride. They interpreted the 70 percent support in the early polls as a guarantee that the measure would pass without their help. By the time it became clear that the vote would be close, it was too late. The good news, perhaps, is that when such measures are undertaken in other states, fewer businesses will fall

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prey to the free-rider temptation. Sweeney's political miracle clearly proves the power of forced dues to change minds.

Unnecessary Provision

Proposition 226 also included a section that required *employers* to get annual written permission before they deduct any money from paychecks for political contributions and expenditures. I believe that this section was totally unnecessary, and it caused major problems. The authors included it to insulate themselves from the charge that the initiative was anti-union. The unions made that charge anyway, claiming they were the only membership organizations affected. More important, the employer section created an opportunity for unions to scare charitable organizations, health-insurance providers, and other groups that receive payroll deductions into believing that they would be hurt by passage of 226.

The union arguments about this provision were disingenuous. First, the initiative applied only to "employers" and "labor organizations" as already defined in California law. No health-insurance provider, except in its role as employer, would be affected. Second, payroll deductions in exchange for something of value, such as health-insurance coverage, would have been excluded according to a previous law. Nevertheless, because this big lie went unanswered in the mass media until the very end of the campaign, many voters believed it was true.

The unions also used this argument with respect to charities; and here, because charitable contributions are not for "consideration," they may have had a point. It is easy to imagine a judge deciding that an employer who deducts voluntary charitable contributions from employee paychecks would be liable for the political expenditures and contributions made by charitable organizations such as the American Cancer Society. If so, many employers would stop gathering charitable contributions that way, and there would be less charitable giving.

That argument convinced some major charities to oppose 226, but they may come to regret their concession. Most people give to support charitable activities, not political causes. The charities' support of the unions seemed to imply that they are involved in politics.

In any case, the exit polls indicated that if the proposition had been written to apply only to unions, it would have passed. The unions were unable effectively to use any part of the section that applied directly to them in their campaign. They argued that it was an effort to silence working people in the political process, but everyone, including most union members, saw through that claim. Workers would have been free to authorize unions to use their dues and fees for political purposes. No limits on voluntary political spending through unions would have been imposed. In fact, by giving workers a choice, the initiative would have amplified the political voice of working people.

There was at least one happy outcome of the campaign. Most California workers are now fully aware of their right, under the Supreme Court decisions in the Hudson (public-sector) and Beck (private-sector) cases, not to have their union dues spent on politics against their will. Until the campaign, unions had tried to keep those decisions a secret. At their behest, President Clinton had rescinded an executive order that would have required federal contractors to post notice of their employees' Beck rights at job sites. During the campaign the unions argued that the Hudson and Beck decisions made 226 unnecessary. Of course, that's untrue, because those decisions are not adequately enforced and they impose a heavy burden on employees to prove that unions spend more money on politics than they admit. But California unions have now informed all their members that these decisions exist and that they all may seek refunds of dues and fees used for politics. I predict a substantial increase in the number of California workers who try to do so in spite of the threats, intimidation, and hurdles the unions will put in their way.

One more thing. The initiative will be back on the primary ballot in 2000 □

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"[When people] say 'let's do something about it,' they mean 'let's get hold of the political machinery so that we can do something to somebody else.' And that somebody is invariably you."

—FRANK CHODOROV (1887–1966)
"Freedom Is Better"

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